ORIGINAL

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman
GARY PIERCE
PAUL NEWMAN
SANDRA D. KENNEDY
BOB STUMP

IN THE MATTER OF THE APPLICATION OF SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC. FOR A HEARING TO DETERMINE THE FAIR VALUE OF ITS PROPERTY FOR RATEMAKING PURPOSES, TO FIX A JUST AND REASONABLE RETURN THEREON, TO APPROVE RATES DESIGNED TO DEVELOP SUCH RETURN AND FOR RELATED APPROVALS.

DOCKET NO. E-01575A-08-0328

NOTICE OF FILING CLOSING BRIEF OF SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC.

Sulphur Springs Valley Electric Cooperative, Inc., through counsel undersigned, hereby files its Closing Brief in the above-captioned matter.

RESPECTFULLY SUBMITTED this 22nd day of May, 2009.

SNELL & WILMER L.L.P.

By [signature]

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ORIGINAL and 13 copies filed this 22nd day of May, 2009, with:

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COPIES of the foregoing hand-delivered
this 22nd day of May, 2009, to:

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COPY of the foregoing sent via E-Mail and U.S. Mail
this 22nd day of May, 2009, to:

Jane Rodda, Administrative Law Judge
Hearing Division
ARIZONA CORPORATION COMMISSION
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By ____________________

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BEFORE THE ARIZONA CORPORATION COMMISSION

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KRISTIN K. MAYES–Chairman
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SANDRA D. KENNEDY
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IN THE MATTER OF THE APPLICATION OF SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC. FOR A HEARING TO DETERMINE THE FAIR VALUE OF ITS PROPERTY FOR RATEMAKING PURPOSES, TO FIX A JUST AND REASONABLE RETURN THEREON, TO APPROVE RATES DESIGNED TO DEVELOP SUCH RETURN AND FOR RELATED APPROVALS.	DOCKET NO. E-01575A-08-0328

CLOSING BRIEF OF

SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC.

May 22, 2009

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I. INTRODUCTION

Sulphur Springs Valley Electric Cooperative, Inc. ("SSVEC" or "Cooperative") is an Arizona member-owned non-profit rural electric distribution cooperative headquartered in Willcox, Arizona. SSVEC is a Class A electric public service corporation that serves most of Cochise County and portions of Santa Cruz, Pima, and Graham Counties, pursuant to a Certificate of Convenience and Necessity issued by the Arizona Corporation Commission ("Commission"). SSVEC's 13-member Board of Directors ("Board") oversees all aspects of the Cooperative's operations and approves the annual operating budget for the Cooperative. At a special meeting of the Board held on June 18, 2008, the Board approved the filing of an application with the Commission for a hearing to determine the fair value of its property for ratemaking purposes, to fix a just and reasonable return thereon, to approve rates designed to develop such return and for related approvals ("Application"). SSVEC is a Class A member of the Arizona Electric Power Cooperative, Inc. ("AEPCO"). On January 1, 2008, SSVEC converted its membership in AEPCO from an All Requirements Member ("ARM") to a Partial Requirements Member ("PRM") pursuant to Commission Decision No. 70105 (December 21, 2007).

On June 30, 2008, the Cooperative filed the Application with the Commission. This was SSVEC's first request to increase its rates and charges in more than 16 years since the Cooperative sought, and obtained, a rate increase pursuant to Decision No. 58358 (July 23, 1993) in Docket No. U-1575-92-220 (the "1993 Rate Decision"). The Application, as originally filed, sought to increase its annual revenue by $10,881,590, which would result in an increase in retail rates of approximately 11.75%. This requested increase was designed to enable the Cooperative to:

- Increase its equity by 1.5% – 2.0% per year to reach the Commission's recommended equity level of 30% by 2014/2015;
- Increase its annual cash flow; and

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- Meet its financial objectives regarding the addition of new generation sources resulting from continuing growth within its service territory.

In addition to, and in conjunction with, the Application, SSVEC requested the Commission approve:

- A revision to its Wholesale Power Cost Adjustment ("WPCA") mechanism to include the pass-through of future generation and transmission costs associated with Cooperative-owned generation and transmission facilities;
- A new Debt-Cost Adjustment mechanism that would permit the Cooperative to recover increases in interest costs associated with Commission-approved financing of plant additions;
- The elimination of line extension credits pursuant to the Cooperative's line extension policy;
- SSVEC's Demand Side Management ("DSM") Program ("DSM Program") (to the extent not already approved);
- The inclusion of a portion of approved future DSM program expenses in base rates with additional expenses and new DSM programs to be recovered through a new DSM Adjustment Mechanism and approval process; and
- Revisions to its Tariffs and Service Conditions.

Following the filing of the Application, on July 30, 2008, the Commission's Utilities Division ("Staff") found the Application to be sufficient and issued its Letter of Sufficiency. During the ensuing months, there was extensive discovery conducted by Staff, the pre-filing of testimony by the Cooperative and Staff, a public comment session held on February 11, 2009, in Sierra Vista, Arizona (which was attended by all five Commissioners), and a public hearing held in Tucson, Arizona, from April 21, 2009 through April 23, 2009, on the Application.

Several of the original requests the Cooperative made in its Application were withdrawn or modified based upon recommendations made by Staff. For example, SSVEC decided not to pursue its request for a Debt-Cost Adjustment Mechanism or to have a portion of its DSM Program expenses included in base rates. However, the most significant issues embodied in the Application, as well as various new issues that arose

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during the rate case process, were discussed at the hearing and are addressed in this Closing Brief.

What is important to note from the outset is that SSVEC is a non-profit member-owned cooperative that has a member-elected Board that oversees the operations of the utility on behalf of the members.[1] As a non-profit cooperative, SSVEC has no shareholders. This makes it fundamentally different than a typical investor-owned utility that has, as one of its objectives, to earn as high a return as possible for the benefit of its shareholders. In the case of a cooperative such as SSVEC, the profit motive is removed and its clear objective is to provide its members safe and reliable service at the *least possible cost.* The Cooperative must collect from its members sufficient rates and charges to operate the utility and have sufficient margin to borrow money to fund capital improvement, and other projects necessary to not only maintain the utility, but to address growth within its service territory. Unlike an investor-owned utility, if the Cooperative was to collect rates and charges from its members in excess of what it needs in order to achieve these objectives, it is required to return the excess to the member-ratepayers through capital credits.

In his Rebuttal Testimony, SSVEC's Member Services Director, Jack Blair, discussed the fundamental differences between an investor-owned utility and a cooperative. Mr. Blair stated:[2]

> Unlike a large investor-owned utility like TEP or APS, as a non-profit community-based cooperative, SSVEC is owned and governed by its member/ratepayers who, therefore, have a direct say in how the Cooperative spends the money it collects through utility rates. In fact, all of the approximately 930 electric cooperatives throughout the US abide by something that is called *The 7 Cooperative Principles* (which I happen to carry around in my wallet). It should be noted that Principal No. 2 is called

[1] This is one of the reasons why the legislature deemed it was not necessary for the Residential Utility Consumer Office ("RUCO") to continue to intervene in cooperative rate case proceedings before the Commission on behalf of residential ratepayers and changed the law in 1994. RUCO was an intervenor in SSVEC's last rate case.

[2] *See* Exhibit A-18, page 12, line 20 through page 13, line 14.

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"Democratic Member Control" which states:

> Cooperatives are democratic organizations controlled by their members who actively participate in setting their policies and making decision. Men and women serving as elected representatives are accountable to the membership. In primary cooperatives, members have full voting rights – one member, one vote, and cooperatives at other levels are organized in a democratic manner.

Principle No. 3, called "Members' Economic Participation", states, in part, that:

> Members contribute equally to, and democratically control, the capital of the cooperative.

Finally, Principle No. 7, entitled "Concern for Community", states:

> While focusing on member needs, cooperatives work for the sustainable development of their communities through policies accepted by their members.

SSVEC believes that its ability to operate for approximately 16 years without asking its members for a rate increase is due to its prudent management practices as described in the Direct Testimony of the Cooperative's CEO, Creden Huber.[3] Although Staff has taken the position in this rate case that perhaps SSVEC's 16-year absence from Commission rate review is not such a good thing, SSVEC believes that to hold rates constant for 16 years and then ask for only an 11.75 percent rate increase is something the Commission should view positively. Accordingly, the Cooperative should not be viewed by the Commission as a utility that is in need of even more regulatory oversight. To the contrary, based upon its actions over the last 16 years, the Cooperative has earned the right to be afforded the benefit of their proven track record in terms of the way it will operate the utility in the future and should not be regulated in such a way that would hinder its ability to achieve its goals and objectives which are designed to benefit its member ratepayers. This is why SSVEC has objected to some of Staff's recommendations, as discussed below.

[3]Exhibit A-2, page 6, line 6 through page 7, line 16.

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Finally, if there is one theme that SSVEC believes permeated throughout this proceeding, it would be that SSVEC needs to come out of this rate case with the ability to build its equity to 30 percent by 2016. To the extent that various Staff recommendations will negatively impact that ability, SSVEC requests that those recommendations either not be adopted or be mitigated for the Cooperative by other acceptable ratemaking means. As the Application currently stands, SSVEC is requesting a rate increase of $9,862,959 and a revenue requirement of $102,688,240. This translates into an increase for the average residential customer of only 10.46% after 16 years. Staff is proposing a rate increase of $7,595,316 and a revenue requirement of $100,420,597. This translates into an increase for the average residential customer of 6.78%. As discussed below, Staff's proposed revenue requirement is not supported by the evidence and, if adopted, would hinder the Cooperative's ability to achieve its operational and financial objectives.

II. THE COOPERATIVE IS ENTITLED TO JUST AND REASONABLE RATES UNDER ARIZONA LAW

The Commission is established by Article 15, Section 1, of the Arizona Constitution. The Commission's authority is derived from Article 15, Section 3, which provides, in pertinent part, that the Commission "shall have full power to, and shall, prescribe just and reasonable classifications to be used and just and reasonable rates and charges to be made and collected, by public service corporations within the State for service rendered therein." Ariz. Const. Art. 15, §3.

When setting rates for public utilities, the Commission should focus on the principle that "total revenue, including income from rates and charges, should be sufficient to meet a utility's operating costs and to give the utility and its stockholders a reasonable rate of return on the utility's investment." *Scates v. Arizona Corp. Comm'n,* 118 Ariz. 531, 533-34, 578 P.2d 612, 614-15 (App. 1978). In the case of a cooperative, the reasonable rate of return relates to the operating margin that the utility needs to achieve its financial and operational objectives consistent with its non-profit status.

Although the Commission's authority to prescribe rates is plenary, (*See, Tucson Elec. Power Co.,* 132 Ariz. at 242, 645 P.2d at 233), the Commission's rate-making authority is subject to the "just and reasonable" clauses of Article 15, Section 3, of the Arizona Constitution. *Residential Utility Consumer Office v. Arizona Corp. Comm'n*, 199 Ariz. 588, 591, 20 P.3d 1169, 1172 (App. 2001). Under most circumstances, the Commission is constitutionally obligated to find the fair value of the [utility's] property and use such finding as a rate base for the purpose of calculating what are *just and reasonable* rates . . . While our Constitution does not establish a formula for arriving at fair value, it does require such value to be found and used as the base in fixing rates. The reasonableness and justness of the rates must be related to this finding of fair value. *Simms v. Round Valley Light & Power Co.,* 80 Ariz. 145, 151, 294 P.2d 378, 382 (1956); *see also Arizona Corp. Comm'n v. Ariz. Pub. Serv. Co.,* 113 Ariz. 368, 370, 555 P.2d 326, 328 (1976); Ariz. Const. art. 15, §14. Further, the *Simms* court stated: "The standard for establishing a rate base must be the fair value of the property and not what the Commission might believe was a fair rate of return on common equity." *Simms*, at 80 Ariz. 145, at 155, 294 P.2d 378, 385; *see also*, *Arizona Corporation Commission v. Arizona Public Service Company*, 113 Ariz. 368, 370, 555 P.2d 326, 328 (1976); *Arizona Corp. Comm'n v. Arizona Water Co.,* 85 Ariz. 198, 203, 335 P.2d 412, 415 (1959); *Scates, supra,* 118 Ariz. 531, 534, 578 P.2d 612,615.

Under the Arizona Constitution as interpreted by this court, the Commission is required to find the fair value of the company's property and use such finding as a rate base for the purpose of determining what are "just and reasonable" rates. *Arizona Corporation Commission v. Arizona Public Service Company*, 113 Ariz. 368, 370, 555 P.2d 326, 328 (1976) (Citing *Simms*, *supra*). Thus, the rates established by the Commission should meet the overall operating costs of the utility and produce a

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reasonable rate of return or margin. It is equally clear that the rates cannot be considered just and reasonable if they fail to produce a reasonable rate of return (or margin for the Cooperative) or if they produce revenue which exceeds a reasonable rate of return. *Scates, supra*, 118 Ariz. 531, 534, 578 P.2d 612, 615.

III. ISSUES WHERE THE COOPERATIVE AND STAFF ARE IN AGREEMENT

In its Application, SSVEC submitted various requests for Staff consideration and Commission approval. In analyzing the Application, Staff agreed with many of those requests and recommended in its direct and/or surrebuttal testimonies (or at the hearing) that such requests be approved by the Commission. Additionally, in its direct and surrebuttal testimonies, Staff made various recommendations to the Commission regarding the Application and other matters that the Cooperative agreed to in its rebuttal and rejoinder testimonies (or at the hearing). Set forth below are what SSVEC considers to be the areas of agreement between the Cooperative and Staff:

A. Approval of Application – Based upon the evidence presented in this proceeding, SSVEC and Staff are in agreement that the Commission should approve the Application consistent with the agreed-upon issues set forth in this Section and subject to a final adjudication by the Commission of the issues in dispute set forth in Section IV herein.

B. Test Year Fair Value Rate Base and Rate Base Adjustments – SSVEC accepted Staff's determination of fair value rate base and all corresponding rate base adjustments, and SSVEC and Staff (collectively the "Parties") have agreed that SSVEC's fair value rate base for the Test Year ended December 31, 2007, to be $132,866,202.[4]

C. Operating Margin Adjustments – The Parties have agreed to the following operating margin adjustments proposed by Staff:

[4] Exhibit S-7, CSB-2 and CSB-3.

•	No. 1	Revenue Annualization -	$ 303,312[5]
•	No. 1	Expense Annualization -	149,184[6]
•	No. 3	2008 Fort Huachuca Contract	0[7]
•	No. 4	Base Cost of Power	10,523,837[8]
•	No. 5	DSM Expenses	(484,966)[9]
•	No. 7	GDS Expenses	(51,427)[10]
•	No. 8	Normalized Legal Expenses	(52,892)[11]
•	No. 11	Interest Expense on LTD	(426,301)[12]
•	No. 12	Capital Credits	(2,722,816)[13]

D. **Capital Structure** – The Parties have agreed that 2016 is a reasonable period to obtain a 30 percent equity-to-long-term debt capitalization ratio.[14] However, as discussed below, the Cooperative disagrees that Staff's proposed revenue requirement will provide sufficient margins to increase SSVEC's equity to 30 percent by 2016.[15]

E. **Reporting of SSVEC's Fuel Adjustor Reports** – SSVEC has agreed to Staff's recommendation that an officer sign the Cooperatives WPFCA (hereinafter defined) reports.[16]

F. **Change in Name of Wholesale Power Cost Adjustment Mechanism** – The Parties have agreed that SSVEC will continue to have a WPCA and that the name of

[5] Exhibit S-7, Schedule CSB-10.
[6] *Id.*
[7] Staff had originally proposed to increase revenues by $918,803 in Exhibit S-6 but subsequently withdrew this adjustment in Exhibit S-7 in recognition of additional information provided by the Cooperative. *See* Exhibit S-7 at page 2, lines 9-21 and CSB-12.
[8] *Id.* at Schedule CSB-13.
[9] *Id.* at Schedule CSB-14.
[10] *Id* at Schedule CSB-16.
[11] *Id.* at Schedule CSB-17.
[12] *Id.* at Schedule CSB-20.
[13] *Id.* at Schedule CSB-21.
[14] *Id* at page 12, lines 1-3.
[15] Exhibit A-9 at page 8, lines 10-14.
[16] Exhibit S-12 at page 14, lines 4-10; Exhibit A-8 at page 1, line 26 through page 2, line 3.

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the WPCA be changed to the Wholesale Power and Fuel Cost Adjustment ("WPFCA").[17]

G. Establishment of Base Cost of Power – Staff has agreed with SSVEC's proposal that the base cost of power for the Cooperative be established at $0.072127 per kWh.[18]

H. Thresholds for the WPFCA – SSVEC has agreed with Staff's recommendation that a $2 million threshold for under-collections and a $1 million threshold for over-collections be established for the WPFCA bank balance.[19]

I. WPFCA Pass-through of Fuel Costs for Owned Generation – Staff has agreed with SSVEC's proposal that fuel costs that may arise if SSVEC were to have its own generation units may be passed through the WPFCA.[20]

J. Cost Components for Inclusion in WPFCA – SSVEC has agreed with Staff's recommendation regarding the fuel and power costs to be included in the WPFCA mechanism.[21]

K. Service Conditions – The Parties have agreed that the Service Conditions proposed in the Application, as modified by Exhibit A-16 (that incorporates Staff's recommended changes) be approved by the Commission. This includes the changes to eliminate the construction allowance for line extensions.[22]

L. Power Procurement Procedures – SSVEC has agreed that within 12 months of the issuance of Commission order in this matter ("Decision"), it will file as a compliance item, written power procurement procedures.[23]

. . .

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[17] Exhibit S-12 at page 13, lines 7-13; Exhibit A-8 at page 1, line 26 through page 2, line 3.
[18] Exhibit S-12 at page 4, lines 13-14; Exhibit A-8 at page 1, line 26 through page 2, line 3.
[19] Exhibit S-12 at page 9, lines 14-16; Exhibit A-9 at page 12, lines 13-15.
[20] Exhibit S-12 at page 10, lines 16-18; page 11 at lines 9-15.
[21] Exhibit S-12 at page 12, lines 9-17; Exhibit A-8 at page 1, line 26 through page 2, line 3.
[22] Exhibit S-12 at page 14, line 12 through page 16, line 16; Exhibit A-8 at page 1, line 26 through page 2, line 3.
[23] Transcript of Hearing ("Trans."). at page 168, lines 16-21.

M. Revenue Allocation and Rate Design – With the exception of the Customer Charges and the Service-Related Charges for Existing Member Connect Fee – Regular Hours and the Non-Pay Trip Fee – Regular Hours charges discussed hereinbelow, and subject to a final determination of the issues in dispute regarding adjustments to the revenue requirement also discussed below, SSVEC has agreed to Staff's revenue allocation and rate design, including Staff's recommended time-of-use rates ("TOU").[24]

N. Tariff Changes – Staff has accepted SSVEC's proposed tariff changes, and SSVEC has agreed that in a future rate case filing, it will develop more detailed and conventional unbundled rates, which will not result in any incentive or disincentive for customers who want to choose competitive generation suppliers.[25]

O. Bill Estimation Tariff – SSVEC has agreed with Staff's recommendation that within 30 days of a Decision in this matter, the Cooperative will file with the Commission a tariff describing its bill estimation methodologies.[26]

P. Revised DSM Program – SSVEC has agreed with Staff's recommendation that SSVEC file with Docket Control a revised version of its DSM Program description having removed references to the TOU rates and controlled rate program for irrigators and make other conforming changes when filing an application for approval of new DSM programs.[27]

Q. New DSM Adjustment Tariff and Assessment of DSM Costs – SSVEC has agreed with Staff's recommendation that costs prudently incurred in connection with Commission-approved DSM activities be recovered entirely through a DSM adjustment tariff.[28] SSVEC has also agreed with Staff's recommendation that Commission-approved

[24] Exhibit S-9 at page 4, line 7 through page 7, line 7; Exhibit A-9 at page 2, line 21.
[25] Exhibit S-8 at Executive Summary, paragraph 2; Exhibit A-8 at page 1, line 26 through page 2, line 3.
[26] Exhibit S-8 at page 12, line 11 through page 13, line 13; Exhibit A-8 at page 1, line 26 through page 2, line 3.
[27] Exhibit S-10 at page 2, line 18 through page 3, line 2; Exhibit A-18 at page 2, lines 6-14.
[28] Exhibit S-10 at page 8, lines 8-11; Exhibit A-18 at page 2, lines 16-22.

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DSM costs be assessed to all SSVEC electric customers as a clearly labeled, single line-item per kWh charge on customer bills.[29]

R. Reporting of DSM Program Expenses – SSVEC and Staff have agreed that SSVEC shall file with Docket Control semi-annual DSM Program Expense Reports by March 1 and September 1 of each year containing the information set forth in Exhibit S-10, at page 14, lines 6-16. The September report will detail DSM Program expenses from January through June, and the March report will report DSM Program expenses from July through December. SSVEC shall redact any personal information, such as the names and addresses, associated with customers participating in the such programs.[30]

S. Annual Adjustor Reset Filing – SSVEC and Staff have agreed that by March 1 of each year, SSVEC shall file with the Commission a request to reset the DSM adjustor, and that the per kWh rate be based upon currently projected DSM costs for that year (the year for which the calculation is being made), adjusted by the previous year's over- or under-collection, divided by projected retail sales (kWh) for that same year.[31]

T. Commission Approval of New DSM Programs[32] – SSVEC and Staff have agreed that new DSM programs shall be submitted to the Commission for approval. SSVEC and Staff have further agreed that SSVEC may commence offering new DSM programs to its members prior to Commission approval and report those expenses as part of its semi-annual reports. However, if the new DSM program is not subsequently approved by the Commission, SSVEC would not be permitted to recover such program expenses. Upon approval of the DSM program, SSVEC would be permitted to recover

[29] Exhibit S-10 at page lines 13-16; Exhibit A-18 at page 3, lines 1-7.

[30] Exhibit S-10 at page 13 line 22 through page 14, line 16; Exhibit S-11 at page 2, lines 11-23; Exhibit A-18 at page 4, lines 1-23.

[31] Exhibit S-10 at page 15 lines 7-22; Exhibit S-11 at page 5, lines 6-8; Exhibit A-18 at page 5 lines 19-23.

[32] As part of its Application, SSVEC submitted three new DSM programs for the Commission to approve in the Decision in this proceeding. At the hearing, Staff indicated that it intended to file Staff's recommendation regarding these new programs prior to the briefing in this matter. SSVEC considers this to be very important as it will impact the final DSM adjustor rate established in the Decision.

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the expenses trued-up to the date it started offering the DSM program at the next annual adjustor reset.[33]

U. **Recovery of DSM Costs for Programs Currently Approved** – SSVEC and Staff have agreed that the initial DSM adjustor rate be set to recover prudently incurred DSM Program costs associated only with approved DSM programs presently in place and that the adjustor rate be set at $0.000256[34] per kWh until the annual reset of the adjustor.[35]

V. **Recovery of DSM Costs for Costs Incurred Prior to 2009** – SSVEC and Staff have agreed that for DSM costs incurred prior to 2009, including the 2006 and 2007 DSM Program costs that have previously been submitted for Staff approval, that such costs continue to be recovered through its WPFCA.[36]

W. **REST Adjustor and Tariff** – SSVEC has agreed to Staff's recommendation that the Commission authorized an adjustor mechanism for SSVEC to replace its REST surcharge and that within 30 days of the date of the Decision in this matter, SSVEC shall file with the Commission a REST Tariff with conforming changes to reflect recovery through the adjustor, rather than through the surcharge used presently.[37]

X. **Cost of Service Study** – Staff has agreed that the Cost of Service Study contained in the Application should be accepted by the Commission.[38]

Y. **Sonoita Reliability Project** – Staff and SSVEC agree that (i) SSVEC has evaluated numerous options regarding the Sonoita Reliability Project (the "Project") and its associated 69 kV line to Sonoita and that the Project will improve reliability in the

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[33] Exhibit S-10 at page 16, lines 4-9; Exhibit S-11 at page 8, lines 5-21; Exhibit A-18 at page 7, line 16 through page 8, line 2.

[34] This amount may be increased if Staff approves the Cooperative's DSM program expenses for 2007 and 2008 as further discussed hereinbelow.

[35] Exhibit S-10 at page 20 lines 21-23; Exhibit A-18 at page 11, lines 2-6.

[36] Exhibit S-10 at page 19 lines 16-25; Exhibit A-18 at page 10, lines 10-22.

[37] Exhibit S-10 at page 22, lines 18-24; Exhibit A-18 at page 11, lines 9-22.

[38] Exhibit S-5 at page 18, lines 19-20.

Sonoita, Patagonia, and Elgin service areas; (ii) SSVEC continues to communicate with its members of such areas through public meetings and mailings to provide a clear indication to such members that the primary issue related to this Project is reliability and quality of service; and (iii) SSVEC should continue to upgrade its 69 kV sub-transmission and distribution system to improve system performance and reliability for its members.[39]

IV. ISSUES WHERE THE COOPERATIVE AND STAFF DISAGREE

A. REVENUE REQUIREMENT ADJUSTMENTS.

Both the Cooperative and Staff are in agreement that SSVEC should obtain a 30 percent equity-to-long-term debt capitalization ratio by the year 2016. To that end, after agreeing to various adjustments made by Staff, SSVEC's proposed revenue requirement is $102,688,240. SSVEC's proposed revenue requirement would produce a return on fair value rate base (referred to as operating margin by Staff) of $16,706,387 for a 12.57 percent rate of return on the agreed-upon original cost rate base of $132,886,202. SSVEC proposed revenue requirement produces a 2.46 net operating TIER and a 2.25 DSC. In contrast, Staff believes that SSVEC can reach 30 percent equity by proposing a revenue requirement of $100,420,597 that would produce an operating margin of $15,365,515 or an 11.56 percent rate of return on the agreed-upon rate base of $132,886.202. Staff asserts that its proposed revenue requirement would result in a 2.34 operating TIER and a 2.12 DSC.

The differences in the two proposals stem from various adjustments and assumptions that Staff has made regarding its proposed revenue requirement. SSVEC believes that the attainment of its recommended revenue requirement from whatever source of revenue is critical for the Cooperative to achieve its financial and operational objectives and requests that the Commission adopt its requested revenue requirement of $102,688,240.

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[39] *Id.*at page 7, lines 11-13, page 19, lines 18-20, and page 20, lines 7-8.

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Although there has been much agreement between the Cooperative and Staff on many issues, the evidence presented at the hearing clearly demonstrates that in order for the Cooperative to have sufficient operating margin to achieve its objectives, including reaching a 30 percent equity level by 2016, the following Staff adjustments to the annual revenue requirement should not be adopted:

1. *__Reduced operating margin resulting from Staff's proposed revenue requirement ($1,340,871) -__*

There is no basis for the reduced operating margins other than to simply lower rates. Moreover, this reduced operating margin will make the agreed-upon stated goal of SSVEC achieving a 30 percent equity level by 2016 impossible. The evidence presented at the hearing clearly demonstrates if Staff's proposed revenue requirement is adopted, SSVEC will not achieve the 30 percent equity level by 2016.[40]

Surrebuttal Schedule CSB-23 to the Surrebuttal Testimony of Crystal Brown (Exhibit S-7) sets forth Staff's equity and long-term debt projections.[41] It should be noted that the top portion of that Schedule is derived from the Cooperative's Rebuttal Exhibit DH-9 attached to Mr. David Hedrick's testimony. Therefore, both the Cooperative and Staff are in agreement with this starting point for this calculation. However, the bottom portion of Surrebuttal Schedule CSB-23 clearly shows where Staff has deviated in order to justify its margin adjustment. In 2009, Staff begins increasing equity by reducing long-term debt by $3 million. The $3 million derives from two adjustments; $918,806 and $2,081,194. Based upon a review of the Surrebuttal Testimony and Surrebuttal Schedule CSB-23, one can not determine from where these adjustments came. Therefore, Staff was asked to explain these two adjustments at the hearing. Ms. Brown testified at the hearing that the $918,806 that Staff had previously agreed SSVEC was entitled to was derived

[40] Trans. at page 388, line 23 through page 401, line 6.
[41] Exhibit S-7 at page 12, lines 18-19.

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from the increase in margin in the Fort Huachuca contract.[42] Staff then arbitrarily assigned that portion of the increase in margin towards reduction of long-term debt.[43] In essence, Staff agreed with the Cooperative that it was entitled to an additional $918,806 in margin expense associated with the Fort Huachuca contract, then took it away from the Cooperative by assigning it to long-term debt reduction in order to arbitrarily inflate the equity ratio.

If there is any doubt that this was an arbitrary adjustment, one just needs to look to the next part of the calculation. When asked where the $2,081,194 came from, Ms. Brown testified that it came from existing margin *or* depreciation expense.[44] Staff admitted that it came up with $2,081,194 because it determined it wanted to decrease long-term debt by $3 million, so after applying the $918,806 adjustment, it simply subtracted that amount to come up with the additional $2,081,194 in order to "back in" to the $3 million reduction. When asked why Staff decided to reduce long-term debt by $3 million, Ms. Brown testified that Staff wanted the Cooperative to contribute $3 million of its own equity to reduce debt, which in turn would increase equity.[45] The major flaw in Staff's analysis is that Staff reduces long-term debt by an arbitrary $3 million amount which is not available. Mr. Hedrick's Rebuttal Exhibit DH-9 already included a reduction in long-term debt by the entire amount of the margin produced under the proposed revenue requirement. Staff's analysis is further flawed because one objectives of this rate case is for the Commission to authorize a revenue requirement that includes a margin component to achieve 30 percent equity by 2016. If Staff's recommendation (which works on paper but does not work in reality) was adopted, the Cooperative would require an additional $3 million of margin to reduce long-term debt; therefore, based on Staff's

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[42] Trans. at page 390, line 5 through page 391, line 11.
[43] *Id.* at page 389, line 21 through page 390 at line 4.
[44] *Id.* at page 391, line 12 through page 394 line 9.
[45] *Id* at page 394, lines 14-19.

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analysis the Cooperative would be $3 million short per year of meeting its margin needs to build equity. When asked if the Cooperative could achieve a 30 percent equity level by 2016 without this adjustment, Ms. Brown agreed that all things being equal, the Cooperative could not achieve this objective by 2016 and it would take considerably longer to attain.[46]

Additionally, Staff arbitrarily reduced long-term debt by an additional 10 percent, or $1,916,057, *starting in 2012* based upon the "bad economy." Ms. Brown testified that Staff does not believe that the Cooperative will grow at the same pace and, therefore, will not have to borrow as much.[47] When asked where the 10 percent came from, Ms. Brown testified that this was based upon "Staff's professional judgment" as to what would happen in the future.[48] Again, this was an arbitrary determination to further reduce long-term debt in order to justify a lowering of the Cooperative's operating margin to mitigate the rate increase. This adjustment is also inconsistent with two undisputed facts. First, Mr. Huber testified that SSVEC's level of capital projects would continue into the future, which would require SSVEC to continue its current level of borrowing.[49] Second, Staff offered no evidence regarding the Cooperative's level of growth or need for plant additions to support its recommendation. With this additional $1.9 million adjustment, Staff has assigned from the margin (that Staff has already agreed that the Cooperative is entitled to) approximately $4.9 million towards long-term debt reductions to artificially inflate the equity level in order to be able to show that SSVEC can reach a 30 percent equity level by 2016. Without these adjustments, Staff acknowledges that SSVEC's attainment of a 30 percent equity level will be significantly delayed. Moreover, based upon Surrebuttal Schedule CSB-23, Staff agreed that the Cooperative's analysis set forth

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[46] *Id.* at page 394, line 20 through page 395, line 5.
[47] *Id.* at page 396 at line 7 through page 397, line 5.
[48] *Id.* at page 397, lines 6-12.
[49] Id. at page 85, line 15 through page 87, line 19.

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in Mr. Hedrick's Rebuttal Exhibit DH-9 is the appropriate starting point for the analysis.

The acceptance of evidence presented by one person over that presented by another is not necessarily decisive because the weight given any of the evidence is within the Commission's discretion, so long as that discretion is not abused. *City of Tucson*, 17 Ariz. App. 477, 480-481, 498 P.2d 551, 554-555. (Citing, *Arizona Corp. Comm'n. v. Arizona Water Co.*, 85 Ariz. 198, 335 P.2d 412 (1959)). It is, however, also well established "that a reasonable judgment concerning all relevant factors is required in determining the fair value of the properties at the time of inquiry." *Id.* (*Citing*, *Arizona Water Co.*, 335 P.2d 412, 414). If the Commission 'refuses to consider all the relevant factors, the fair value of the properties cannot have been determined under our Constitution.' Mere speculation and arbitrary conclusions are not substantial evidence and cannot be determinative. *City of Tucson v. Citizens Utilities Water Company*, 17 Ariz. App. 477, 481, 498 P.2d 551, 555 (Ct. App. 1972) (Emphasis added.)

The net result of Staff's proposed margin adjustments reduces the annual revenue requirement by $1,340,871. The evidence presented overwhelmingly demonstrates that Staff's proposed operating margin adjustment is arbitrarily determined for the sole purpose of lowering the rates and not supported by the evidence. Accordingly, it should not be adopted.

2. *Payroll Expense Adjustment ($523,570) -*

Staff's reduction of known and measurable payroll expenses post-test year is not appropriate. Staff reduced payroll expenses by $523,570 as a result of the Cooperative's inclusion of 10 employees that were hired after the Test Year in 2008. Staff stated it was not appropriate to include the additional 10 employees because there was a corresponding reduction in staff by employees leaving the Cooperative.[50] Unfortunately, this is not supported by the facts in this case. As Mr. Hedrick testified in his Rebuttal Testimony, (i)

[50] Exhibit S-6 a t page 18, lines 14-17.

the reduction was due to seasonal or part-time employees leaving, and that the staffing level included in the Application shows a net gain of 10 employees; (ii) the payroll level proposed by SSVEC is representative of the known, measureable, and continuing level of payroll expenses needed to provide quality of service to members; and (iii) the Cooperative experienced significant growth over the past five years. Accordingly, the number of employees is reasonable and necessary in order to serve the members.[51]

In response to this argument, Staff noted that the payroll costs outside of the Test Year, were not known and measurable, and would violate the matching of revenues and expenses.[52] However in his Rejoinder Testimony, Mr. Hedrick reiterated that (i) these employees were hired shortly after the end of the Test Year so that the Cooperative could continue to maintain a high level of reliable service; (ii) it was not unreasonable to include these costs in light of SSVEC's margins, equity, and other indicators; and (iii) they are known and measurable payroll costs.[53]

As noted by Staff, A.A.C. R14-2-103.A.3.i states that pro forma adjustments are "adjustments of actual Test Year results to obtain a more realistic relationship between revenues, expenses, and rate base." There is nothing that precludes the Commission from recognizing post-Test Year pro forma adjustments. At the hearing, Staff acknowledged that "post year adjustments are appropriate in circumstances so long as they provide a more realistic relationship between revenue and expenses." The 10 employees at issue were hired in April of 2008, less than four months after the end of the Test Year and are on the payroll today. But because they were hired outside of the Test Year, Staff maintains that it is inappropriate to include the expenses associated with those employees in SSVEC's revenue requirement. However, Staff itself made a pro forma adjustment to interest expense that occurred in November 2008, <u>11 months</u> after the end of the Test Year

[51] Exhibit A-8 at page 8, line 9 through page 9, line 23.
[52] Exhibit S-7 at page 3 line 24 through page 5, line 17.
[53] Exhibit A-9 at page 3, lines 3-23.

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to provide a more realistic relationship between expenses and rate base and because Staff believed that the expense was reflective of reasonable interest expense for SSVEC going forward.[54]

If Staff considers an interest expense that occurred 11 months after the Test Year to be known and measurable, it is inconsistent to say that 10 employees that were hired a mere four months out of the Test Year that are still on the payroll today are not a known and measurable expense. Moreover, Staff admits that because these 10 employees are on the payroll today, SSVEC would have to continue paying these employees from its margins.[55] If this adjustment is adopted, its margin would be reduced by an additional $523,570, thereby further inhibiting the Cooperative's ability to attain its agreed-upon goal of achieving a 30 percent level by 2016. Also, the reduction in operating margin would impact SSVEC's operating cash as these salaries will still need to be paid. Accordingly, this adjustment should not be adopted.

3. *Charitable Contribution Adjustment ($298,622) –*

Staff's reduction of charitable contribution expense is contrary to the 1993 Rate Decision in which the Commission carefully considered this issue and expressly allowed for recovery of such expenses. Staff recommended this adjustment on the basis that "contributions and donations are voluntary costs and, therefore, not needed for the provision of service. Further Decision No. 58358 does not provide for automatic recovery of such costs."[56] Staff further cites to AEPCO agreeing in its last rate case to Staff's recommendation to disallow this expense.[57]

First, AEPCO is not a distribution cooperative. It is a wholesale provider of electricity and its member-ratepayers are companies such as SSVEC. Second,

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[54] *Id.* at page 372, line 13 through page 373, line 14; Exhibit S-6 at page 21, lines 23-25.
[55] Trans. at page 387, line 9-16.
[56] Exhibit S-7 at page 8, lines 8-10.
[57] *Id.* at lines 1-4.

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recognizing that "with a cooperative ratepayers cannot be separated from their member-owners," the Commission specifically looked at this issue in the last rate case and did expressly allow for the recovery of such expenses so long as SSVEC first had its members approve an amendment to the Cooperative's by-laws that permitted the donations.[58] The evidence presented at the hearing clearly demonstrates that (i) the Cooperative initiated that by-law change in 1997, (ii) that the Cooperative filed the proposed change to its by-laws with the Commission's Director of Utilities; (iii) that the by-law change was submitted to the Cooperative's members and was approved by over a 90 percent margin; and (iv) SSVEC donations and sponsorship programs have been widely accepted and acclaimed by its members.[59]

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Mr. Blair testified to one of the primary cooperative principles, which is:

> While focusing on member needs, cooperatives work for the sustainable development of their communities through policies accepted by their members.[60]

Mr. Blair went on to testify that:

> Over the 70 year history of SSVEC, the Cooperative has always shown its commitment to the community through charitable donations and sponsorships in the areas that we serve. This ensures that member dollars stay in the community. Although the dollar amount at issue is quite small, (less than .3 percent of total revenue), the benefits to our members and the local non-profit organizations are great. As the Commissioners heard first hand at the February 11, 2009, public comment session on this rate case from numerous community leaders, the donations and sponsorships that the Cooperative make are integral to improving the qualify of life for our members in our service territory. These donations and sponsorships, such as the Boys and Girls Scouts, hospital foundations and organization, youth sports teams, money raising events for education and medical equipment for hospitals, are just a few of the kinds of organizations and sponsorships that SSVEC supports.[61]

[58] *See* 1993 Rate Decision at page 18, line 27 through page 19, line 18.
[59] Exhibit A-18 at page 13, line 15 through page 16, line 8; Rebuttal Exhibits JB -1 and JB-2; *See* also Tr. page 341 line 7 through page 348, line 4.
[60] Exhibit A-18 at page 13, lines 11-13.
[61] *Id.* at page 13, line 15 through page 14, line 2.

This is a very important issue for the Cooperative as it underscores better than any other issue the difference between an investor-owned utility and a member-owned cooperative and the role that a cooperative has in the rural community. If the SSVEC members were unwilling to support its Cooperative's ability to maintain these programs in favor of either lower rates or a return through capital credits, they would have not approved the by-law change by such an overwhelming margin. Moreover, if the members decide they do not want the Cooperative to continue such programs, they can initiate such a change through the Board. Given the analysis that the Commission did in its last rate case, as well as the fact that if the adjustment is adopted, the Cooperative will have to pay for these programs from its margin (which is inconsistent with the agreed-upon goal of SSVEC reaching a 30 percent equity level by 2016), this proposed adjustment should not be adopted.

4. *Rate Case Expenses Adjustment ($59,522) –*

At the time of the filing of the Application, the Cooperative had included in its annual revenue requirement $20,000 ($100,000 of expenses amortized over five (5) years) which reflected the approximate amount of expenses the Cooperative had incurred. Regarding rate case expenses, SSVEC witness Rebecca Payne testified as follows:

> Rate Case Expense (Schedule A-9.0). An adjustment to recognize expense associated with the development, filing and support of the rate case has been made. The estimated cost of $100,000 is intended to reflect cost of outside legal and consulting services. This amount amortized over a 5-year period, resulting in an adjustment of $20,000. Actual rate case expense will only be known at the time of the hearing/settlement. Schedule RAP-2 shows invoices related to this case incurred up to the filing. We propose to file invoices to ACC Staff for all additional rate case related expenses for a final determination of rate case expense. (Emphasis added.)[62]

Staff made no mention of Ms. Payne's testimony in its Direct Testimony and simply included reflected the $20,000 in rate case expenses as part of Staff's recommended revenue requirement. Consistent with Ms. Payne's testimony cited above,

[62] Exhibit A-15 at page 7, lines 3-11.

in his Rebuttal Testimony, Mr. Hedrick testified as follows: [63]

> Q. Is it appropriate to include an adjustment to reflect the additional rate case expense incurred by SSVEC?
>
> A. Yes. Typically, the total amount of rate case expenses incurred is allowed to be recovered. An adjustment is necessary to reflect the additional amount incurred by SSVEC above the amount already included in the adjusted test year expenses.
>
> Q. Please explain the adjustment SSVEC is proposing.
>
> A. SSVEC included an adjustment for $100,000 for rate case expenses in the original Application. Amortized over a 5-year period, the annual increase included in test year expenses is $20,000.
>
> As of February 27, 2009, SSVEC has incurred $310,608 for legal and consulting rate case expenses. In addition to the actual rate case expenses incurred to date, SSVEC estimates there will be an additional cost of $87,000 through the completion of the hearing. SSVEC requests rate case expenses of $397,608 be allowed. Amortized over a five-year period, the adjusted rate case expense is $79,522. SSVEC requests expenses be increased by $59,522 to reflect the additional rate case expense. Schedule Exhibit DH-7 is provided in support of this adjustment.

In response to this testimony, Staff issued data request 16.1 requesting (Exhibit A-22) invoices for legal expenses that had been incurred. SSVEC provided Staff with copies of legal invoices from February 2008 through February 2009. Yet, after reviewing the supporting documentation, in Staff's Surrebuttal Testimony it refused to recognize the additional rate case expenses on the basis that SSVEC had not prepared a "budget of anticipated costs" and disallowed the additional $59,522 of rate case expenses.[64]

In response, Mr. Hedrick testified in his Rejoinder Testimony as follows:[65]

> Q. What is Staff's argument for not including the actual rate case expenses incurred?
>
> A. Staff argues that because SSVEC did not have a budget and did not (in Staff's opinion) provide careful analysis of costs, SSVEC is entitled only to the recovery of the initial estimate of rate case expenses.

[63] Exhibit A-8 at page 12, lines 1-21.
[64] Exhibit S-7 at page 10, lines 4-20.
[65] Exhibit A-9 at page 6, line 1 through page 8, line 8.

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Q. Is Staff's argument reasonable?

A. No. The lack of a budget and analysis of the costs is not the reason for the increase in the rate case expenses. SSVEC's rate case expense adjustment included in the filing represented the estimate of rate case expenses up to the time of the filing. SSVEC filed the Application in this rate case in June 2008. Since that time, the Cooperative has responded to 17 sets of formal data requests that comprised 274 questions (not counting subparts) and provided in excess of 15,000 pages of information in both hard copy and electronic form. SSVEC staff, consultants, and attorneys have spent many hours preparing responses to both formal and informal requests for information from Staff. In addition, SSVEC' staff, consultants, and attorneys have spent many hours preparing Rebuttal (and now Rejoinder) Testimony and have met with Staff regarding DSM and other issues. Finally, because Staff determined in December of 2008 to hire a rate case consultant to provide testimony relating to SSVEC's power procurement activities, SSVEC had no choice but to engage an additional consultant to assist in data request responses and to provide Rebuttal analysis and testimony.

In response to Staff's data request CSB 16.1, SSVEC provided, and Staff reviewed, actual invoices of legal and consulting expenses from February 2008 through February 2009 totaling $331,527, which the Cooperative has already paid. In March 2009, SSVEC was invoiced an additional $23,893 and $8,718 in legal and consulting expenses, respectively. And, through April 15, 2009, SSVEC has incurred additional legal expenses of $20,681. Therefore, as of April 15, 2009, SSVEC has incurred known and verifiable rate case expenses totaling at least $384,819. These amounts do not include the additional legal and consulting rate case expenses that SSVEC will be required to incur related to completion of its Rejoinder Testimony and Witness Summaries, hearing preparation, the actual rate case hearing, and closing briefs. Therefore, SSVEC will incur rate case expenses well in excess of the $397,608 that has been requested.

As an electric cooperative, SSVEC does not have a rate department of employees to deal with all of the filings and issues in a rate case. Cooperatives typically do not have frequent rate cases, therefore maintaining in-house resources to handle rate cases is not prudent. Instead, SSVEC and other cooperatives rely on outside consultants and attorneys to provide the necessary expertise. SSVEC has not had a rate case in 17 years. There are many issues that have been raised in this case which have required more effort by all parties involved. SSVEC has no control over the level of involvement and discovery pursued by Staff in this proceeding. SSVEC is required to respond to Staff requests for information. Staff's assertion that SSVEC has been guilty of poor planning and lacking in its control of rate case costs would appear to be misplaced.

Additional evidence is provided showing that the Commission has

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allowed comparable levels of rate case expenses for utilities of even smaller size than SSVEC. Attached as Rejoinder Exhibit DH-1.0 is a list of the rate case expenses approved by the Commission in ten other proceedings over the last five (5) years. Given the level of effort required to comply with Commission filing requirements and Staff discovery, it is not appropriate to deny the recovery of the actual and reasonable expected rate case expenses incurred. A denial of this request will result in a further reduction in SSVEC's available margin as the expenses must be paid. Accordingly, SSVEC continues to request that the revenue requirement be increased by an additional $59,522 to $79,522, amortized over five (5) years, so that the Cooperative has the opportunity to recover most (not all) of the rate case expenses that it will incur to complete this rate case.

At the hearing, SSVEC spent considerable time cross-examining Ms. Brown on Staff's recommendations. Some of the issues that Ms. Brown acknowledged were that:

- The Cooperative had provided Staff copies of invoices for rate case expenses through February 2009, totaling $331,527, consistent with Ms. Payne's testimony;[66]
- Staff had reviewed those invoices and did not find any problem with them.[67]
- The Commission has in the past awarded more rate case expenses than what was requested in the initial Application;[68]
- For an investor-owned utility, shareholders would bear the cost of unrecovered rate case expenses, where as for a cooperative, it would be the member ratepayers that would bear the cost.[69]
- Although SSVEC had incurred rate case expenses totaling $384,819 as of April 15, 2009, it had not increased its recovery request despite having to incur additional expenses for Rejoinder Testimony, the hearing, briefing, etc.[70]
- When the Cooperative was preparing its rate case, it had no way of knowing how many data requests would be issued, how many witnesses there would be for the hearing or what additional issues would be interjected into the rate case proceeding.[71]

. . .

[66] Trans. at page 401, line 15 through page 402, line 25; page 409, line 20 through page 410, line 20; Exhibit A-8 at page 6, lines 24-26.
[67] Trans. at page 422, lines 19-25.
[68] *Id.* at page 403, lines 10-19.
[69] *Id.* at page 403, line 25 through page 404, line 7.
[70] *Id.* at page 410, line 21 through page 411, line 25.
[71] *Id.* at page 414, line 4 through page 419, line 15.

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- The Company offered to amortize its rate case expenses over five years as opposed to three or four years, which has been more typical.[72]
- The total amount of rate case expenses will exceed $400,0000, and SSVEC requested reimbursement for only $397,606.[73]
- The SSVEC rate case could not be conducted for $100,000.[74]
- The Cooperative had no choice but to answer the 17 sets of data requests propounded by Staff and could not refuse to answer them even if it had prepared a budget;[75]
- Staff was willing to approve rate case expenses for the pending Trico rate case in excess of $100,000, despite being a much smaller case with fewer issues.[76]
- If Staff's recommendation was adopted, SSVEC would have to pay its rate case expenses from operating margin.[77]

As Mr. Hedrick testified at the hearing, given the circumstances with respect to this rate case, even if SSVEC had prepared a budget, it would not have made any difference whatsoever in terms of reducing or controlling rate case expenses. It is Staff and the Commission that largely control the rate case process once the Application is filed and not the Cooperative.[78] Moreover, various issues arose in this rate case that could not have been predicted from the outset including, but not limited to: (i) the shear number of data requests propounded by (17 sets and 268 questions)[79]; (ii) the need for the Cooperative to engage a power procurement witness in response to Staff hiring Mr. Mendl; (iii) a three-day (as opposed to a one-day or two-day) hearing; (iv) the interjection of the 69 kV line issue; (iv) an additional public comment session; and (v) additional issues initiated by Staff, such as the recommendations for the Commission to approve WPFCA increases and the dispute relating to the DSM adjustor reset.

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[72] *Id.* at page 423, lines 5-18.
[73] *Id.* at page 424, lines 5-18.
[74] *Id.* at page 424 line 24 through page 25, line 7.
[75] *Id.* at page 414, line 25 through page 415, line5.
[76] *Id.* at page 426, line 22 through page 428, line 7.
[77] *Id.* at page 428, lines 9-21.
[78] Exhibit A-9 at page 7, lines 7-21; Trans. at page 222, lines 9-14.
[79] Exhibit A-23.

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The issue of the recovery of rate case expenses has been discussed by the Commission in several recent rate case decisions. Although Black Mountain Sewer Corporation ("BMSC") is a much smaller company than SSVEC with only a $1.3 million revenue requirement (as opposed to over a $100 million for SSVEC) and only approximately 2,000 customers (as opposed to approximately 50,000 for SSVEC), the Commission found in Decision No. 69164 (December 5, 2006) that BMSC (like SSVEC) had initially estimated its rate case expenses indicated it would true-up costs as the case progressed. Additionally, and similar to the unanticipated issues that arose in the SSVEC case, additional rate case expenses were approved for BMSC because of the unexpected intervention of two additional parties, as well as more extensive discovery than expected. Regarding these events, the Commission stated in its decision that:

> . . . to hold a company strictly to its original estimate, regardless of intervening events, would create an incentive for over-estimating costs on the front, rather than attempting to provide a good faith estimate subject to reconciliation based on actual events. We do not believe Staff or RUCO's proposals provide adequate recognition of the additional costs incurred by BMSC in procuring its rate case, and we will, therefore, adopt the Company's position on this issue.[80]

In the UNS Electric Case (Decision No. 70360, May 27, 2008), the Commission recognized that there are certain circumstances based upon the facts of the case that justify higher levels of rate case expense recovery. The decision found that:

> Although Staff and RUCO present strong arguments in support of their recommendations, given that this is the first UNSE rate case since the acquisition of the Citizens assets, and that UNSE was required to respond to a substantial number of data requests, we will allow rate case expenses of $300,000, normalized over three years.[81]

This is SSVEC's first rate case in 16 years. Additionally, it is uncontroverted that SSVEC was required to respond to a substantial number of data requests. The Commission has recognized that these situations may be taken into consideration.

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[80] Decision No. 69164 at page

[81] Decision No. 70360 at page 24, lines 8-11.

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In Decision No. 67093, June 30, 2004, for Arizona-American Water Company, (with approximately $10 million revenue requirement and only 15,000 customers), the Company requested rate case expenses totaling $715,000. Decision No. 67093 describes how the company's Director of Rates and Planning for the five western states of American Waterworks testified that that the company had a number of rate cases going on at the same time and did not have the internal resources to handle them. The Commission went on to find that: [82]

> As explained in the recent Arizona Water Company Decision No. 66849 (March 19, 2004), while we do not believe it is unreasonable for a company to retain outside counsel or consultants to prepare and litigate rate case filings, at some point the utility must mitigate the costs associated with retaining those services. . . . Based upon our review of the complexity of this proceeding, the number of systems involved in the rate request, and a comparison of other cases, we find that rate case expenses in the amount of $418,941 is reasonable for this proceeding.

In Rejoinder Exhibit DH 1.0 to Mr. Hedrick's Rejoinder Testimony, which is also attached hereto as Attachment A, the Cooperative submitted evidence of a representative sample of cases where the Commission awarded rate case expenses. It should be noted that all of those cases amortized rate case expenses over three (3) or four (4) years, where SSVEC proposed amortizing its expenses over five (5) years to help mitigate the rate impact. The Cooperative also provided as a late-filed exhibit, Exhibit A-28, which broke down the rate case expenses incurred by month and by professional consultant. Staff has presented no controverting evidence to any of the evidence presented by SSVEC with the exception of its belief that $100,000 is appropriate because SSVEC did not prepare a budget.

Finally, at the hearing, the following question was posed to Staff and the following answer was given:[83]

[82] Decision No. 67093 at page 20, lines 11-19.
[83] Trans. at page 425 line 24 through page 426 line 7.

Q. Okay. And given your -- the answer to my question before about the fact that you agree that this case could not be done for $100,000, isn't Staff's recommendation, isn't it true that Staff's recommendation to maintain this $100,000, which is really only reflective of the amount of expenses it incurred up to the time of the filing, isn't it somewhat punitive?

A. No. Staff believes that is a normal level of ongoing rate case expense that should be included in the revenue requirement, and that not including the amount over $100,000 would not harm the customers and would result in lower rates.

In light of the uncontroverted evidence presented, the $100,000 does <u>not</u> reflect "a normal level of ongoing rate case expenses. If SSVEC is not permitted to recover its rate case expenses, this will serve to only lower SSVEC's equity because the expenses will come out of SSVEC's margin which is inconsistent with one of the primary agreed-upon goals of this rate case proceeding. Moreover, when the Commission has considered rate case expense recovery in the past, as indicated in the decisions cited above, the primary factors are what are the actual expenses, what are the specific facts and circumstances of the case, and what has the Commission done in other cases. None of these cases disallowed reasonable rate case expense because the utility did not prepare a budget before filing its rate case.

On the basis of the overwhelming evidence presented on this issue supporting the Cooperative's position and the fact that the Cooperative has not requested (nor will it recover) all of its rate case expenses for this proceeding, SSVEC respectfully requests that Staff's recommendation that only $20,000 be included for rate case expenses be rejected and that the annual revenue requirement include a total of $79,522 for such expenses.

5. <u>*Christmas and Safety Pay Adjustment ($45,058) -*</u>

Staff has characterized these payments as "incentive based" and not necessary to provide safe and reliable service and should be paid from SSVEC's margins.[84] However, Staff does not object to the Cooperative recovering expenses for fair and reasonable

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[84] Exhibit S-6 at page 21, lines 1-8; Exhibit S-7 at page 8, line 22 through page 9, line 5.

compensation.[85] Practically speaking, and looking past what these payments are called, to what they actually are, the evidence demonstrates that these payments have not been treated by the Cooperative as incentive based and should, therefore, be considered as part of the employees' compensation package. Although the Cooperative is not required to pay these amounts, they have been consistently paid each year and during the Test Year and were paid to all 195 employees.[86]

With respect to the safety pay, maintaining the highest level of safety is an important objective of the Cooperative. The $24,557 was the amount paid during 2007 to all 195 employees with the average payment being only $126.[87] In SSVEC's last rate case, the Commission found "that the Cooperative has shown this expense to be appropriate and of benefit to the Cooperative's ratepayers and will not disallow it."[88]

Regarding the Christmas pay, the $20,500 of expense results in a $100 payment to employees during the Test Year and is a routine and expected part of the employees' compensation.[89]

Staff has recommended that these expenses be paid from SSVEC's internally generated cash flows. This would have the effect of further reducing SSVEC's margin, which is inconsistent with the goal of achieving a 30 percent equity level by 2016.[90] Accordingly, the Commission should not adopt Staff's proposed adjustment for these payments.

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[85] Trans. at page 367, lines 13-19.
[86] Exhibit A-8 at page 11, lines 10-23; Exhibit A-9 at page 4, lines 11-18.
[87] Exhibit A-8 at page 11, lines 16-19.
[88] 1993 Rate Decision at page 14, lines 4-6.
[89] Exhibit A-8 at page 11, lines 21-23.
[90] Exhibit S-7 at page 9, lines 2-5; *See* also Trans. at page 369, lines 17 through page 370, line 25. Although Ms. Brown suggests that this could also be paid from the Cooperative's depreciation expense, she provided no support for SSVEC being required to do this as both SSVEC and Staff had previously agreed on the amount of depreciation expense that SSVEC was entitled to recover.

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B. THE COOPERATIVE SHOULD NOT BE REQUIRED TO SEEK COMMISSION APPROVAL EACH AND EVERY TIME IT DETERMINES IT MUST INCREASE THE WPFCA.

1. *Staff's recommendation is unnecessary and overly burdensome to the Cooperative and should not be adopted.*

Currently, SSVEC has a WPCA that the Commission established in the 1993 Rate Decision that permits the Cooperative to pass through fuel and purchased power costs to its members. Up until January 2008, SSVEC was an ARM and obtained all of its power from AEPCO through a similar adjustment mechanism that AEPCO has to pass through its costs to its member distribution cooperatives. In January 2008, pursuant to Commission approval, SSVEC became a PRM of AEPCO, which entitles SSVEC to now obtain a portion of its power from sources other than AEPCO which, at some time in the future, may include self-generation. However, notwithstanding becoming a PRM, SSVEC will still obtain approximately 80 percent of its power needs from AEPCO, and it is anticipated that through 2012, SSVEC will obtain between 75.3 and 88.3 percent of its power from AEPCO.[91] Additionally, as Mr. Brian testified, when a large power contract comes back to AEPCO in 2011, SSVEC could obtain as much as 94 percent of its power from AEPCO:[92]

> And Sulphur, I mean we have talked about Sulphur buying 80 percent of its power from AEPCO. That number actually goes up over time over the next few years because the entitlement from AEPCO grows as one of the contractual sales that AEPCO is obligated to expire.
>
> There is a 100 megawatt sale to Salt River Project, for example, that would bring about 30 more megawatts of base load power to Sulphur in the year 2011. So the 80 percent number actually goes up about 94 percent in 2011. So we are talking about a very small amount of power in the scheme of things for a very small rural cooperative.

As with all of the AEPCO member distribution cooperatives, SSVEC has no

[91] Exhibit S-13 at page 3, lines 12-25.
[92] Trans. at page 183, line 18 through page 184, line 4.

control over the cost AEPCO passes through and has no choice but to pay such amounts. However, the AEPCO adjustor mechanism is monitored and approved by the Commission through semi-annual filings that AEPCO makes with the Commission.

Staff recommended that since SSVEC became a PRM in January of 2008:[93]

> [t]he Cooperative's energy costs have become more volatile. The greater the volatility impacts the bank balance and, consequently, the WPCA rate. In order to manage the WPCA rate, Staff recommends that, in the future, SSVEC submit proposed increases to the WPCA rate to the Commission for approval. Submitting proposed increases for approval would ensure that impacts to the Cooperative's customers are regulated.
>
> Staff does not recommend that SSVEC be required to seek approval for decreases in the WPCA rate.

Moreover, Staff's recommendation applies to *all* increases, even if the increase will not result in any customer "rate shock" whatsoever and no matter how miniscule the increase. For example, if SSVEC sought to increase its adjustor by 1 percent and there was a $1.00 (or less) increase to the customer, SSVEC would be required to expend the time and expense necessary to file for Commission approval and wait many months for such approval. This would (i) negatively impact the ability of the Cooperative to properly administer its bank balance; (ii) require the Cooperative to use its equity margin to "lay out" the money to purchase the power (that as a public utility it is obligated to acquire) for extended periods of time; (iii) spend time, money, and resources going through a Commission proceeding (just to implement a small increase); (iv) cause significant delay in the Cooperative's ability to recover costs; and (v) hinder the Cooperative's ability to be in compliance with the under-collection bank balance threshold. Requiring Commission approval defeats the purpose of the adjustor mechanism which is to allow timely recovery of wholesale costs incurred that are outside the Cooperative's control.[94]

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[93] Exhibit S-12 at page 7, lines 24 through page 8, line 3.
[94] Exhibit A-8 at page 18, line 25 through page 19, line 2.

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As also discussed below, both Staff witness Jerry Mendl, and SSVEC witness, David Brian, were in agreement that 2008 was a very anomalous and anon-representative year because of high energy prices as (i) in 2008, oil prices reached $147 per barrel based on worldwide demand and concerns about Iraq and a weak dollar; and (ii) power prices followed natural gas prices, peaking at approximately $125/MWh.[95] It also just happened to be the first year that SSVEC was a PRM, and the Cooperative was in the process of transitioning from an ARM to a PRM. Finally, in light of the fact that the Cooperative will be obtaining between 75 and 88 percent (or more) of its power from AEPCO, and SSVEC does not control the cost of that power, Staff's recommendation will result in the Commission duplicating its efforts by reviewing power costs twice because the majority of such costs will have already been reviewed for AEPCO prior to the pass-through to SSVEC.

Staff is also concerned that the Cooperative could purchase less than 80 percent of its power from AEPCO.[96] This concern is unfounded because the only time the Cooperative would do this is when the cost of AEPCO is more expensive that what the Cooperative could obtain by going to the market. If this happens, the amount of purchased power expenses that will be included in the WPFCA will be less resulting in a benefit to the members.

If Staff's primary concern is truly the avoidance of "rate shock" for customers, Staff has proposed, and the Cooperative has already agreed, that a $2 million threshold for under-collections and a $1 million threshold for over-collections be established for the WPFCA bank balance.[97] This mechanism will help ensure that the bank balance does not grow to a level that will cause rate shock when the Cooperative increases its adjustor.

[95] Exhibit A-5 at page 30, lines 22-23; *See* also Exhibit DMB-8 of Exhibit A-5; Trans. at page 174, lines 21 through 24; Trans. at page 184, line 21 through page 185, line 2; *See* also Trans. at page 128, lines 12-19.
[96] Exhibit S-13 at page 3, lines 12-18.
[97] Exhibit S-12 at page 9, lines 14-16; Exhibit A-9 at page 12, lines 13-15.

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The Cooperative clearly demonstrated to the Commission that over the last 16 years, it has operated the utility in a prudent manner to cut costs and keep rates as low as possible for its members for as long as possible.[98] Additionally, Staff has acknowledged that that purchased power prices that SSVEC paid in 2008 during the January through October timeframe were not likely to be representative of purchased power prices in 2009.[99] Rather than require the Cooperative to file for approval for increases at this time, the Commission should give the benefit of the doubt to the Cooperative and its management and allow additional time to operate as a PRM under more normal and representative circumstances than what occurred in 2008. Additionally, the Commission should allow additional time to see if the thresholds that have been agreed to will alleviate the rate shock concern. SSVEC believes that Staff's recommendation is simply an overreaction to a finite situation that existed in 2008 and should not be adopted.

2. *<u>The Cooperative has proposed a reasonable alternative that will achieve Staff's objective</u>.*

If Staff's primary concern is the avoidance of "rate shock" for customers, in addition to the thresholds that the Cooperative has already agreed to, SSVEC has proposed a reasonable compromise position. This position takes into consideration the issue discussed above relating to the Cooperative being forced to file for very small increases that will not result in customer rate shock. As discussed by Mr. Hedrick in his Rebuttal Testimony:[100]

> SSVEC understands the concerns of Staff regarding the level of increase that can result from an increase in the WPCA rate. In order to address these concerns, SSVEC proposes the following:
>
> That SSVEC be allowed to adjust its WPCA rate without Commission approval unless such adjustment would result in a

[98] Exhibit A-2 page 6, line 8 through page 7, line 16.
[99] Trans. at page 128, lines 12-19
[100] Exhibit A-8 at page 19 line 15 through page 20, line 2.

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> cumulative annual increase in the total average rate collected from customers per kWh greater than 10%. Increases submitted to the Commission for approval in excess of the 10% limit would become effective in 60 days unless the Commission took action.
>
> This provision would allow SSVEC a timely recovery of the routine fluctuations in fuel cost without Commission approval. It would also ensure that no significant increase or "rate shock" is implemented unless approved by the Commission.

When asked about Staff's concern about the Cooperative's proposal for the 10 percent limit, Staff testified as follows:

> There are a number of issues with the company's recommendation on how the 10 percent limit would function. One of them is that there is no way to know what the actual impact would be on customers' bills because we do not know going forward what the cost of fuel is going to be, particularly over the course of years. Another problem with the company's proposal is that it is unduly complex and it would be difficult to track in terms of compliance with that 10 percent limit that they are recommending. And, finally, it is, because of its complexity, really not likely to be transparent to ratepayers. It is, it is difficult to understand.[101]

First, if the impact on the customer bill was going to be greater than 10 percent, the Cooperative would have to file for approval consistent with the mechanism that Staff is proposing. At that point, the Commission would have the same ability to review and limit the amount of the increase consistent with what Staff is currently proposing. Second, the cost of fuel going forward is irrelevant to the mechanism. The cost is the cost, and if the increase will result in less than a 10 percent increase, the Cooperative would not be required to file for Commission approval; if the increase is greater than 10 percent, the Cooperative would file for approval, and the Commission would exercise the oversight that Staff is already proposing. Third, the Cooperative proposed this mechanism because it is not "unduly complex" or "difficult to understand." As Mr. Hedrick testified as cited above, the Cooperative would file for Commission approval of the increase if the "adjustment would result in a cumulative annual increase in the total average rate

[101] Trans. at page 598, lines 2-15.

collected from customers per kWh greater than 10 percent." At the hearing, Administrative Law Judge ("ALJ") Rodda asked Mr. Hedrick the following question, and Mr. Hedrick answered as follows:[102]

> Q. All right. So then you talked also about a 10 percent yearly band or impact on it. And then you were talking about customer bill. Wouldn't it be different for every customer? What are you talking about, an average customer?
>
> A. Yes. The way that I had envisioned it and what we had provided to the Staff was that the average cost per kilowatt hour for the entire system we could calculate. So to the extent that the wholesale power cost adjuster results in an average increase in the cost that customers are paying greater than 10 percent, we would have to get Commission approval for that. So we would reduce the amount that customers are paying to a cost per kilowatt hour. And to the extent that assumes that we are proposing an increase to the wholesale power cost adjuster, let's assume that the average cost is 10 cents a kilowatt hour on average, that's what everybody pays, and we are proposing an increase to the wholesale power cost adjuster of 5 mils, so it is 5 percent, we wouldn't have to get Commission approval. Let's say we do that in March and we come back in June and say, well, we need an additional penny. Well, that puts us at well above 10 percent in terms of the increase. We would have to go to the Commission to get approval for the amount in excess of the 10 percent. We would be limited to implementing a wholesale power cost adjustment that affected customer bills of 10 percent without Commission approval.
>
> Q. Is that a rolling 12-month period?
>
> A. Yes.

The proposed mechanism is not overly complex and can certainly be worked out with Staff and memorialized in a tariff if the Commission adopts the Cooperative's compromise position relating to the filing of increases.

3. *If the Commission requires SSVEC to file for increases in the WPFCA, the agreed-upon WPFCA rate should be considered an initial ceiling for adjustment purposes.*

Staff has agreed with SSVEC's proposal that the base cost of power for the Cooperative be set at $0.072127 per kWh and that SSVEC's be able to continue its

[102] Trans. at page 286, lines 13 through page 287, line 18.

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WPFCA for recovery of expenses in excess of this amount.[103] Accordingly, in adopting these rates, the Commission has determined this to be a just and reasonable rate. Staff has proposed that the Cooperative must obtain Commission approval for <u>any and all</u> increases in the WPFCA. At the hearing, Staff was asked to clarify its position (on what it meant by any and all increases) to determine whether the recommendation means an increase *above* the initial adjustor rate that will be established following the Decision, or increases in the adjustor rate following a decrease that does not exceed the initial adjustor rate: [104]

> Q. Okay. Let me give you a hypothetical, because this is where I am still struggling to understand how this is going to work. Let's say in a given year Sulphur has lowered -- the adjustor level is set and let's say it translates into 2 cents, just for -- okay, it is 2 cents. So the number that is approved in this Commission allows for a 2 cent adjustor. Now, Sulphur needs to lower that adjustor to 1 cent. All right? And it stays at 1 cent for a period. Okay? Then Sulphur incurred some fuel costs and then it needs to raise it back to 2 cents. All right? Would you agree with me that the 2 cents established in this rate decision would be considered the ceiling in that Sulphur would only have to come in for increases beyond the 2 cents?
>
> A. No.
>
> Q. Okay. So once -- and again I am only asking because we really weren't sure what you meant here. If the Commission is establishing the adjustor at 2 cents hypothetically, or whatever that decimal, long decimal number is, and lowers it, Staff is unwilling to allow the company to go back up to that amount, the amount established in this rate case decision, without coming to the Commission first?
>
> A. Staff's position is that any increase to the adjustor must be filed with the Commission for approval.
>
> Q. Okay. That clarifies it. And, again, in your testimony you stated that the reason that, one of reasons Staff is recommending that the Commission approve all increases is to mitigate potential rate shock?
>
> A. That is correct.

This position makes no practical sense. First, in the Decision that will be issued in this proceeding, the Commission will approve the WPFCA thereby finding the initial rate

[103] Exhibit S-12 at page 4, lines 13-14; Exhibit A-8 at page 1, line 26 through page 2, line 3.
[104] Trans. at page 610, lines 4 through page 611, line 10.

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factor derived from the Decision to be just and reasonable. Staff has proposed, and the Cooperative has agreed, that SSVEC will not need to obtain Commission approval to lower the adjustor rate. If the Cooperative lowers the adjustor rate below the initial adjustor rate, under Staff's proposal, the lowered rate now becomes the new ceiling and SSVEC is precluded from raising the adjustor above that new rate without obtaining Commission approval, even though it is less than the initial rate established as a just and reasonable rate. Second, if SSVEC was to increase the now lowered adjustor rate back to the initial rate, there would be no rate shock, as the rates would simply return to the level set by the Commission in this rate case which was found to be just and reasonable. Accordingly, SSVEC should be permitted to raise the adjustor back to the initial rate factor that will be in effect following the Decision without Commission approval. Only increases above that rate should require Commission approval, as opposed to <u>any and all</u> rate increases of the WPFCA as proposed by Staff.

Additionally, if the Cooperative files for an increase in its adjustor rate and the Commission approves a new increased adjustor rate above the rate derived from the Decision, that rate should supplant the initial adjustor rate derived from the Decision as the new ceiling for purposes of future increases and decreases of the WPFCA.

SSVEC requests that if the Cooperative is required to seek Commission approval for increases in the WPFCA, the mechanism established be consistent with what SSVEC has proposed above.

4. <u>*If the Commission requires the Cooperative to file for an increase in its WPFCA, the increase should go into effect if the Commission does not act upon the filing within 60 days*</u>.

If the Commission determined that SSVEC must file for increases in its WPFCA, because timely recovery of expenses are critical to the Cooperative, SSVEC has proposed a mechanism that the Commission has authorized in the past that will ensure the Commission's ability to review and approve the increase in a timely manner, as such

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review and approval process is out of the Cooperative's control. In his Rebuttal Testimony, Mr. Hedrick testified as follows:

> Increases submitted to the Commission for approval in excess of the 10% limit would become effective in 60 days unless the Commission took action.... This provision would allow SSVEC a timely recovery of the routine fluctuations in fuel cost without Commission approval.[105]

In his Rejoinder Testimony, Mr. Hedrick further testified to this point, as follows:

> SSVEC also believes that there must be some provision that requires the Commission to act on such filings within a specified time frame. Given the magnitude of the wholesale power cost and the potential impact of a less than timely recovery, a 60-day turn-around is not an unreasonable expectation. Staff suggests that the Cooperative could file six (6) months in advance to avoid a lag in recovery. Staff also testifies that purchased power costs are volatile and hard to predict. SSVEC is dependent upon AEPCO for the majority of its purchases and market prices for the remainder. SSVEC is not always able to predict changes in power cost into the future. That is why the WPCA factor is so important in the recovery of these costs. Unlike an investor-owned utility that may be able to predict fuel costs well into the future, SSVEC does not have that same ability. It is essential that SSVEC have the ability to recover sudden increases in fuel costs without a significant delay at the Commission.[106]

Staff, however, objected to this proposal, stating that:

> Market conditions can change or new question can arise concerning an application. Under such circumstances, a 60-day limit could potentially limit the Commission's ability to fully consider an increase before it went into effect.[107]

On cross-examination, however, Staff admitted that it can typically take as long as four to five months for the Commission to approve an adjustor reset.[108] Moreover, Staff further provided information in its response to data request SSVEC 1.6 that the Commission has previously approved adjustors for three other utilities that go into effect unless suspended by the Commission.[109] Those utilities are AEPCO (Decision No.

[105] Exhibit A-8 at page 19 lines 21-25.
[106] Exhibit A-9 at page 13, lines 22 through page 14, line 8.
[107] Exhibit S-13 at page 5, lines 17-19.
[108] Trans. at page 539, lines 7-16.
[109] *Id.* at page 641, lines 2 through 642 line 6.

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68071, August 17, 2005), Arizona Public Service (Decision No. 6963), and UNS Electric (Decision No. 70360, May 27, 2008). A copy of Staff's response to SSVEC 1.6 is attached hereto as Attachment B.

In light of (i) SSVEC being a cooperative (as opposed to an investor-owned utility) that must have timely recovery of its fuel and purchased power costs and the timing of the Commission approval process is out of SSVEC's direct control; (ii) in the near future, between 75 percent and 88 percent (or more) of its power will come from AEPCO, and the Commission will have already approved the pass-through of those costs to SSVEC; and (iii) the Commission precedent that has already allowed a automatic adjustors for other utilities (including a cooperative) if the Commission does not act, SSVEC requests that if the Commission requires SSVEC to file for adjustor increases, such increases be permitted to go into effect if the Commission does not act to suspend the Cooperative's filing within 60 days.

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5. *If the Commission requires the Cooperative to file for an increase in its WPFCA, power purchased from AEPCO that is passed through the Commission-approved AEPCO adjustor should not be considered for purposes of an increase to the WPFCA*.

As discussed in detail above, SSVEC has, and will continue to obtain most of its power from AEPCO for the foreseeable future. AEPCO passes through the costs associated with its power purchased for SSVEC by way of a Commission-approved pass-through adjustor mechanism. Therefore, SSVEC has no control over the costs that AEPCO passes through which have already been reviewed and approved by the Commission. Accordingly, if the Commission decides to require SSVEC to file for increases in its WPFCA, in light of the thresholds that the Cooperative has agreed to, such filing should only be for those increases resulting from SSVEC's power purchases from non-AEPCO sources.[110]

[110] Exhibit A-9 at page 19, lines 2-10.

6. ***The $453,347 of DSM Program expenses for 2007 and 2008 should be excluded for purposes of increases in the WPFCA and the $2 million under-recovery threshold level.***

Staff has agreed with SSVEC's proposal that the base cost of power for the Cooperative be established in the Decision issued in this proceeding for the WPFCA to be $0.072127 per kWh.[111] Staff has proposed that the Cooperative must obtain Commission approval for <u>any and all</u> increases in the adjustor. At the hearing, Staff was asked to clarify its position on this to determine whether the recommendation includes an increase in the adjustor rate resulting from Staff's approval for recovery of the $453,347 of 2007 and 2008 DSM Program expenses that have been submitted for Staff approval and are currently pending (and discussed in more detail in Section IV.D below.) Moreover, as reflected in III.V above, Staff and the Cooperative have agreed that for DSM costs incurred prior to 2009, including the 2007 and 2008 Program costs that have previously been submitted for Staff approval, such costs continue to be recovered through its WPFCA.[112] At the hearing, Staff was asked to clarify its position on whether this amount would be included for purposes of Commission approval for increases in the WPFCA and the $2 million agreed-upon under-collection threshold: [113]

> Q. Okay. Now, just to digress for a moment, right now as part of the DSM recommendation actually, once the 2007 and 2008 program costs are approved, which we heard Mr. Irvine say hopefully will be within the next two, three weeks, which is about $453,000 roughly, that such cost be recovered through the existing adjustor mechanism that's in place now, the wholesale power adjustor, as opposed to the new DSM adjustor. That's your understanding?
>
> A. That's my understanding.
>
> Q. Okay. Now, and this is one of the points of clarification I am trying to get, now, because once these program costs are approved, they are going to go into the existing wholesale power adjustor that we are talking about, right?

[111] Exhibit S-12 at page 4, lines 13-14; Exhibit A-8 at page 1, line 26 through page 2, line 3.
[112] Exhibit S-10 at page 19 lines 16-25; Exhibit A-18 at page 10, lines 10-22.
[113] Trans. at page 608, line 1 through page 609, line 18.

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A. Yes.

Q. Now, the $450,000 of DSM expenses, would Sulphur have to -- are you counting that, meaning would Sulphur have to come to the Commission to increase the adjustor as it relates to those expenses?

A. If it brings the bank balance to the $2 million level or above, yes.

Q. Okay. So in terms of trying to wrap up, the 2 million would include anything that the Commission has approved to go into it anyway? I mean, do you see where I am going with this?

A. If Sulphur, if Sulphur feels that it must increase the adjustor in order to address these costs, then, yes, they would be part of it.

Q. Okay. And, but you would agree that those costs, those costs then of course, once they are recovered, they are gone and they are out and then we are done?

A. Yes.

Q. You know, and I guess the question that we, that the company wanted to ask you about this is that, you know, against this $453,000 is this temporary thing to finish off under the old rate case decision, whether or not Staff could agree that this wouldn't count towards the $2 million, at least initially.

A. Staff does not agree.

Q. Okay. That's what I wanted to get the clarification on.

This is another recommendation that makes no practical sense. By approving the recovery of the DSM expenses, Staff is already determining that the expenses are reasonable and should be recovered. Moreover, Staff is recommending that those expenses be recovered through the WPFCA. These expenses were incurred in 2007 and 2008 and will be run through the WPFCA pursuant to the 1993 Rate Decision and once recovered, will be gone and all future DSM expenses will be recovered through the new DSM adjustor established in this proceeding. The inclusion of an additional $453,347 in the Cooperative's bank balance will not cause "rate shock" and is a temporary "clean-up" measure to transition from the prior 1993 Rate Decision to the Decision that is issued in this matter. Accordingly, SSVEC should not be penalized by having these amounts held against it for purposes of the $2 million under-collection threshold or trigger a filing with the Commission for approval of an adjustor increase. The fair and appropriate treatment of these expenses under the circumstances should be that they are excluded for purposes of those calculations.

C. THE COOPERATIVE SHOULD NOT BE REQUIRED TO FILE FOR A PRUDENCY REVIEW OF ITS POWER PROCUREMENT ACTIVITIES.

In his Surrebuttal Testimony, Mr. Mendl (on behalf of Staff) recommended that the Commission Staff conduct a prudency review of SSVEC's purchased power procurement processes in the next rate case or within three years, whichever comes first.[114] What is interesting to note is that Mr. Mendl did not include this recommendation in his Direct Testimony. It was made in his Surrebuttal Testimony after reading the Rebuttal Testimony of Mr. Brian. Mr. Mendl testified as follows:[115]

> Q. Has Mr. Brian's testimony regarding SSVEC's organizational structure and power procurement procedures caused you to modify your recommendations and conclusions?
>
> A. No, I have not modified my recommendations pertaining to organizational structure and power procurement based on my review of Mr. Brian's testimony.
>
> However, Mr. Brian's testimony has caused me to modify my conclusions. My initial review of SSVEC's organizational structure and power procurement procedures led me to conclude that some improvements were required, but that SSVEC was in transition and was in the process of developing, implementing and refining its power procurement procedures. I believe that SSVEC was open to upgrading and documenting its power procurement procedures, and would be making a good faith effort to do so as it gained more experience with new responsibilities.

. . .

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114 Exhibit S-3 at page 2, lines 13-15.

115 *Id.* at page 12, lines 16 through page 13, line 11.

> Mr. Brian's testimony suggests otherwise, namely his belief that formalized, written, and documented procedures are inappropriate. If Mr. Brian has his way, <u>I now conclude that SSVEC will not make the improvements to its organizational structure and power procurement procedures.</u>
>
> <u>Therefore, I am now augmenting my recommendation</u> to suggest that the Commission Staff conduct a prudence review of SSVEC's purchased power procurement activities in the next rate case, or within three years, whichever comes first. (Emphasis added.)

Based upon this testimony, it appears that Mr. Mendl's subsequent recommendation for a prudency review stemmed solely from his belief based upon his reading of Mr. Brian's Rebuttal Testimony and appears to be somewhat punitive. However, the following should be noted. First, in Mr. Brian's Rejoinder Testimony, he clarifies that:

> ...SSVEC is receptive to reducing its procurement process to written form, if" (a) flexibility can be maintained, and (b) the costs of implementing and maintaining those procedures are not overly burdensome to the Cooperative.[116]

Second, at the hearing, Mr. Brian testified that SSVEC would agree to file as a compliance item written power procurement procedures within 12 months of the Decision in this matter.[117] He also discussed the role of the Western Area Power Administration ("Western") as "Sulphur's trading desk" and Western's important role in assisting SSVEC on power procurement issues.[118]

Based upon this evidence, the basis for Mr. Mendl augmenting his testimony to include this additional recommendation is now moot. Notwithstanding, SSVEC presented additional evidence that demonstrates that it should not be required to submit to a prudency review because it is not necessary or appropriate under the circumstances. It includes the following:

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[116] Exhibit A-6 at page 11, lines 24 through page 12, line 2.
[117] Trans. at page 168, lines 16-21.
[118] *Id.* at page 175, lines 25 through page 178 line 5.

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- SSVEC currently purchases only approximately 20 percent of its power needs from the wholesale markets. The remainder and vast majority of SSVEC's power comes from and will continue to come from AEPCO.[119] SSVEC anticipates that in the foreseeable future, it will obtain in excess of 80 percent of its power from AEPCO. In 2011, SSVEC could buy as much as 94 percent of its baseload power from AEPCO.[120] Moreover, 90 percent of the power from AEPCO is priced at the average pooled rate for all AEPCO members, including ARMs.[121] As the Commission must first approve the pass-through of the AEPCO cost of power to SSVEC, there is no reason for Staff to conduct a prudency review associated with 80 percent or more of SSVEC's purchased power costs when the Commission has already reviewed those costs when authorizing the pass-through, and SSVEC has no choice but to pay for those costs.

- As a non-profit cooperative, unlike an investor-owned utility, SSVEC's only incentive is to procure its supplemental power needs at the lowest possible costs. Hindsight is always twenty/twenty, and, even if it is subsequently determined that a lower cost of power was available at the time, SSVEC must still pass the cost of its power through to its members. There are no shareholders to shield the members from such costs, which exist for an investor-owned utility. If SSVEC's members disagree with the Cooperative's decisions regarding power procurement or otherwise, they have the right and ability to replace the Board.

- SSVEC just became a PRM of AEPCO in 2008. Both Mr. Brian and Mr. Mendl agreed that 2008 was an anomalous year in terms of high energy prices as (i) in 2008, oil prices reached $147 per barrel based on worldwide demand and concerns about Iraq and a weak dollar; and (ii) power prices followed natural gas prices, peaking at approximately $125/MWh.[122]

- Staff acknowledged that purchased power prices that SSVEC paid in 2008 during the January through October timeframe were not likely to be representative of purchased power prices in 2009.[123]

- SSVEC already makes regular filings with the Commission every month relating to the status of fuel and purchased power adjustments, and the Commission is able to review SSVEC's purchased power costs within that existing framework.[124]

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[119] Exhibit A-6 at page 11, lines 16-18.
[120] Trans. page 183, line 18 through page 184, line 4.
[121] *Id.* at page 186 line 20 through page 187, line 14.
[122] Exhibit A-5 at page 30, lines 22-23; *See* also Exhibit DMB-8 to Exhibit A-5; Trans. at page 174, lines 21 through 24; Trans. at page 184, line 21 through page 185, line 2.
[123] Trans. at page 128, lines 12-19.
[124] Exhibit A-6 at page 13, line 23-26.

- The Commission already requires SSVEC to follow a solicitation process for purchases of two years or longer that necessitates Commission oversight and the use of an independent monitor (embodied in Commission Decision No. 70032).[125]

SSVEC believes that based upon the evidence presented as discussed above, Staff's recommendation for the imposition of additional regulatory requirements are unnecessary and will cause SSVEC to have to devote additional and significant time and expense to comply. Like the recommendation for SSVEC to be required to file for an increase in its WPFCA, SSVEC believes that this recommendation is an overreaction to an anomalous and "perfect storm" set of circumstances that arose in 2008, which just happened to be the year that the Cooperative became a PRM and filed its first rate case in more than 16 years. Accordingly, until sufficient time has gone by for the Commission to be in a better position to judge SSVEC's power procurement activities, the Commission should not adopt Staff's recommendation for a prudency review on such a small amount of non-AEPCO purchased power.

D. THE ANNUAL DSM ADJUSTOR RESET SHOULD BE DEEMED APPROVED IF THE COMMISSION DOES NOT ACT BY JUNE 1.

There is no question that among Arizona electric utilities, the Commission has recognized that SSVEC has been very proactive with respect to its DSM and renewable programs.[126] As discussed in Section III above, SSVEC and Staff are in agreement on almost all issues related to DSM. The only issue in which the Cooperative and Staff disagree is the procedural mechanism for the annual reset of the new DSM adjustor.

The Parties have agreed that by March 1 of each year, SSVEC would file for a reset of its DSM adjustor. However, Staff has proposed that the reset of the adjustor become effective on June 1 after Commission approval.[127] Although the Cooperative does

[125] *Id.* at page 14, lines 1-6.
[126] Trans. at page 546, lines 6-13.
[127] Exhibit S-11 at page 7, lines 8-9.

not disagree with this *per se*, its concern is that it is unlikely that the Commission will actually be in a position to approve the filing on or before June 1 of each year.[128] Therefore, SSVEC proposes that if the Commission does not act on the filing by June 1, the adjustor be automatically reset.[129] Staff opposed an automatic reset of the adjustor and testified as follows:

> Staff does not recommend that the DSM adjustor rate take effect automatically. As mentioned previously in Direct Testimony, adjudication of the filing by the Commission will allow the Commission to directly manage recovery of the DSM adjustor rate and the impact it has on ratepayers. Since changes to the DSM adjustor rate have a direct impact on customer bills, it is appropriate that the adjustor rate be set pursuant to Order of the Commission. Automatic implementation as a result of the Commission not consistent with the setting the rate pursuant to Order of the Commission. Staff continues to support Recommendation No. 9, which is that SSVEC's annually proposed new DSM adjustor rate become effective on June 1st after approval by the Commission.[130]

In response to Staff witness Irvine's testimony quoted above, SSVEC witness Blair testified as follows: [131]

> Q. What is SSVEC's concern with this recommendation?
>
> A. As I stated in my Rebuttal Testimony, SSVEC agrees that the new DSM adjustor rate become effective on June 1 of each year. However, Staff is recommending that such effectiveness be contingent upon Commission approval of the reset. Although SSVEC does not oppose the Commission approving the reset, SSVEC believes that the Commission should treat the June 1 date as a "hard" deadline. As more fully explained in my Rebuttal Testimony, Staff will have 90 days to review SSVEC's filing and submit the matter to the Commission for approval on or before June 1st of each year. SSVEC has no control over this process and has no assurance that Staff will conduct its analysis within the timeframe in order to submit a proposed order to the Commission for approval before June 1. SSVEC believes that if the Commission does not approve the filing by June 1, the new adjustor rate should

[128] It should be noted that Staff originally proposed that the Cooperative file on or before April 1 of each year, but it was the Cooperative that proposed filing by March 1 of each year to give Staff and the Commission more time to analyze and approve the filing. *See* A-18 at page 5, line 25 through page 6, line 13.

[129] Exhibit A-18 at page 6, line 15 through page 7, line 13.

[130] Exhibit S-11 at page 7, lines 18-26.

[131] Exhibit A-19 at page 2, line 14 through page 3 line 18.

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At the hearing, Mr. Irvine acknowledged the following:

- If the Commission did not approve the filing by June 1, the adjustor would not be reset.[133]
- It can typically take as long as four to five months for the Commission to approve an adjustor reset.[134]
- DSM Program expenses that SSVEC incurred in the prior calendar year could not be recovered until such time as the Commission acted;[135]
- The process of Staff review and Commission approval is completely outside of the control of the Cooperative (assuming SSVEC is timely with the filing and its responses to data requests).[136]
- From the period 2001 through 2006, SSVEC had semi-annually submitted for Staff approval of $549,929 of DSM Program expenses per the mechanism established in the last rate case decision that it took Staff until July 8, 2008, to approve $502,414 of such expenses.[137]
- SSVEC has submitted for Staff approval its 2007 and 2008 Program expenses on a semi-annual basis totaling approximately $453,000, and Staff has still not acted upon the filings.[138]
- In order for SSVEC to complete its recovery of DSM Program expenses totaling approximately $453,000 incurred for 2007 and 2008 through its WPFCA and have a "clean slate" on a going forward basis, Staff indicated that it was hoping to finish its review by the time briefs are filed.[139]
- If the adjustor went into effect automatically in a given year, the Commission could true-up the adjustor the following year for the two-year period, thereby continuing its oversight over the adjustor although it would be over two years, instead of one.[140]
- If the Commission adopts SSVEC's request for an automatic reset of the adjustor on June 1, and if the Commission does not act, then the adoption of this mechanism would be embodied in the Decision of the Commission that derives from this rate case proceeding.[141]

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[133] Trans. at page 559 lines 19 through page 560 at line 1.
[134] *Id.* at page 539, lines 7-16.
[135] *Id.* at page 561, line 15 through page 562, line 10.
[136] *Id.* at page 562, line 11 through 564, line 1.
[137] *Id* at page 564, lines 5 through page 566, line 1; Exhibit A-24 and A-25.
[138] Trans. at page 566, line 1 through page 567, line 3.
[139] *Id.* at page 574 line 22 through page 575, line 17.
[140] *Id.* at page 568, line 19 through page 570, line 9.
[141] *Id* at page 572, lines 1-22.

Each of the points listed above directly refute the rationale that form the basis of Staff's opposition to SSVEC's proposal and/or illustrate the Cooperative's concern as to why the DSM adjustor reset should not be an open-ended process. It can be reasonably inferred by Staff's testimony that it is unlikely that the Commission will be in a position to approve the adjustor by June 1, yet it proposed a mechanism that is predicated on Commission approval by such date. Moreover, in response to a question by the ALJ that the seven-year approval for the 2001 through 2006 DSM Program expenses was an anomaly,[142] Staff has still not approved the more recent 2007 and 2008 DSM Program expenses.[143]

What this demonstrates is the Cooperative's reticence for an approval process that is primarily out of the Cooperative's control. Although Staff suggested that the Cooperative could file even earlier than March 1, given that the filing would be for Program expenses incurred the previous calendar year ending December 31, it is unlikely that given the Cooperative's resource constraints and other deadlines, it could realistically file any sooner than March 1. Also, given the Cooperative's demonstrated commitment and expenditures to DSM programs, it is not in a financial position to "lay out" money for extended periods of time while it waits for Commission approval. SSVEC believes that its proposal for automatic implementation of the adjustor reset is a reasonable compromise that still provides the Commission with the opportunity to exercise its oversight over the adjustor consistent with its regulatory responsibilities.

Finally, at the hearing, there was discussion that although SSVEC would be obligated to file for an adjustor reset at least annually by March 1, it could perhaps file more often that once a year if it so needed.[144] SSVEC requests that there be language in

[142] *Id.* at page 578, lines 6-10.
[143] Staff has indicated that it might be able to approve these expenses prior to the close of the record in this proceeding.
[144] *See* Trans. at page 581, line 15 through page 583, line 3.

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the Recommended Opinion and Order ("ROO") that would not preclude SSVEC from filing more than once a year if the Cooperative deemed it necessary.

E. THE COMMISSION SHOULD ADOPT SSVEC'S PROPOSED CUSTOMER CHARGES.

SSVEC's proposed customer charges are set forth in the Application (Exhibit A-1, Schedule 0-1.0). SSVEC has proposed increasing the customer charge for residential customers by $5.00 from the current $7.50 charge (established in 1993) to $12.50, which brings the charge closer to its actual cost of $23.31.[145] Staff has proposed that the customer charged be increased by *only* $0.75 to $8.25. Staff's recommendation is based, in part, on trying to limit the increase of this particular charge to approximately 10 percent consistent with the overall proposed revenue increase. Staff asserts that SSVEC's proposed increase results in a 67 percent increase in the charge.

Staff's analysis and recommendation should be rejected for the following reasons:

- SSVEC's proposed charge brings the charge closer to its actual cost.[146]
- To say that it represents a 67 percent increase, although technically accurate if a customer had no kWh usage and his electric bill was only the customer charge of $7.50 per month, is misleading because it singles out only one component of the requested rate increase. The charge should not be looked at in a vacuum but factored in with the overall requested rate increase.
- The Commission has previously approved increases in customer charges for other cooperatives which are similar to those requested by SSVEC. TRICO Electric Cooperative and Navopache Electric Cooperative both received substantial increases in the customer charge component of the rate in their last rate filings before the Commission. The approved change in the residential rate for these cooperatives is:[147]

	Existing	Approved
TRICO	$ 8.00	$12.00
Navopache	$11.25	$18.30

[145] Exhibit A-1, Schedule M-1.0.
[146] Exhibit A-8 at page20, lines 6-25.
[147] *Id.* at page 21, lines 8-17.

- Under Mr. Musgrove's principle of "gradualism", it would take over 20 rate changes to reach the actual $23.31 cost of providing the service if the rate could only be increased by $.075 per rate case.[148]
- As SSVEC has agreed that in a future rate case filing, it will develop more detailed and conventional unbundled rates,[149] moving the charge closer to actual costs is the first step in this process.

Based upon this evidence, Staff's recommendation is not reasonable and the Cooperative's proposed customer charges should be adopted.

F. <u>**THE COMMISSION SHOULD ADOPT SSVEC'S PROPOSED $50 CHARGE FOR REGULAR HOUR CONNECTIONS AND NON-PAY TRIPS**</u>.

The Cooperative and Staff have agreed to all of SSVEC's proposed service-related charges with the exception of (i) the regular hour connection fee; and (ii) the regular hour non-pay trip fee.[150] In both instances, SSVEC has proposed that the Commission approve a $50 charge, and Staff has proposed that the charge be set at $40. The current charge for these two services is $25 and was established in SSVEC's 1993 Rate Decision. Mr. Hedrick testified that Staff's proposed rates do not recognize the actual cost of providing the services, which the Cooperative believes to be $94.78 and $138.29, respectively.[151] Moreover, Staff's approach to setting the rate <u>only</u> took into consideration the increase in the cost of labor since 1993 (and no other factors) without regard to whether the rate established in 1993 covered the Cooperative's actual cost of providing the service. To the extent the Cooperative was not recovering its costs in 1993, it is not the appropriate starting point to set the rate in 2009. Mr. Musgrove testified that the rates established in 1993 were the starting point for his review, and when asked whether Staff assumed that the charges established in 1993 reflected the recovery of SSVEC's costs associated with providing the service, Mr. Musgrove replied "I never made such assumption."[152] Mr.

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[148] Exhibit A-9 at page 14, line 23 through page 15, line 2.
[149] Exhibit S-8 at page 11, line 23 through page 12, line 2.
[150] Trans. at page 478, line 19 through page 481, line 22.
[151] Exhibit A-8 at page 24, lines 10-15; Exhibit A-8, DH-21.
[152] Trans. page 511, lines 22 through page 512, line 5.

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Hedrick further testified that "the Commission has expressed the intent that to the extent practicable, the costs of providing service should be borne by those that cause the costs to be incurred" and that "the establishment of appropriate service is a clear way to accomplish this objective."[153]

SSVEC believes that that the additional $10 increase in these two service charges to $50 moves the charge closer to the actual cost of providing the service[154] and helps to mitigate need for the Cooperative to subsidize the costs from other sources, such as equity.

V. THE SONOITA RELIABILITY PROJECT

SSVEC has been assiduously working toward a solution to bring quality, reliable power to the Sonoita/Elgin/Patagonia communities. The Project has taken years of planning, analysis, design consideration, cost estimation, community participation, and review, and provided SSVEC the information necessary to make sound decisions based upon a balance of community concerns and requirements of the Cooperative with respect to its obligation to provide safe and reliable service within its service territory. As initially identified, the solution to this area's reliability issues is a new substation in Sonoita. Based upon the Community's concerns, SSVEC obtained a new substation property in a commercial land use area of Sonoita, rather than using its existing parcel in a residential subdivision. [155]

The 69 kV sub-transmission line necessary to energize the substation has been the most contentious and emotional issue for the Project. The routing of this line has been the primary focus of the community, and SSVEC has conducted numerous community meetings, met with representative groups and individual property owners, welcomed presentations to its Board, and received e-mails and letters with opinions regarding the

[153] Exhibit A-9 at page 17, lines 22 through 26.
[154] *Id.* at page 17, lines 26 through page 18, line 1.
[155] *See* Exhibit A-3.

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line location.[156] There has also been considerable public comment filed in this rate case docket, as well as oral public comments.

As a non-partisan entity, SSVEC compiled the route arguments and balanced such with basic aspects of business practices and cost analysis. With these facts in mind, SSVEC has determined that the final route for the 69 kV sub-transmission line will follow the existing easement along the San Ignacio del Babocomari Land Grant ("SIDB"). The SIDB easement and affiliated easements to SSVEC's original substation property, Buchanan, have been on record for more than a quarter of a century.[157]

SSVEC's 1982 purchase of nearly twenty miles of SIDB easement, along with utilizing designated utility corridors, has allowed SSVEC to significantly reduce overall project costs due to acquisition of rights-of-way. SSVEC reviewed various other options for the Project, a description and cost estimate for each option is set forth in late-filed Exhibit A-26 which is also attached hereto as Attachment C. SSVEC presented evidence at the hearing that provided reliability and outage information, and provided copies of correspondence to the Commission and its members.[158]

Mr. Creden Huber testified at the hearing regarding issues generally associated with the Project and the 69 kV line in particular. He presented evidence demonstrating that the Sonoita area has had a 10-year average of 270 hours of outages per year because of the unreliability of the existing line. Mr. Huber testified as to his concerns that the community would continue to be plagued by outages if SSVEC did not move forward in soon with the Project and for his concern for the elderly and for the businesses that are impacted. Mr. Huber further testified that renewable energy will not solve this problem as this is a capacity and reliability issue and that the 69 kV line is not the reason that the

[156] *Id.*
[157] *Id.*
[158] *Id.*

Cooperative filed for a rate increase.[159]

Mr. Jack Blair also testified at the hearing that the option SSVEC chose for the siting of the 69 kV line is the only viable option, and the Cooperative has, and will do, everything it can to mitigate the impacts of this line on the surrounding property owners and described some of those plans.[160] Mr. Blair further testified that any further delay in this Project will increase the cost of the Project and prolong the advent of outages that will occur in the area and that it would be necessary for the Cooperative to institute a new hook-up moratorium since the existing line is already at capacity. Finally, Mr. Blair testified that he believes the option SSVEC chose will impact the least amount of members at the lowest possible cost and if the costs were to increase, they would have to be spread out among all of SSVEC's members.[161]

Staff looked at the Project and agreed with SSVEC that: (i) SSVEC has evaluated numerous options regarding the Project and its associated 69 kV line to Sonoita and the Project will improve reliability in the Sonoita, Patagonia, and Elgin service areas; (ii) SSVEC continues to communicate with its members of such areas through public meetings and mailings to provide a clear indication to such members that the primary issue related to this Project is reliability and quality of service; and (iii) SSVEC should continue to upgrade its 69 kV sub-transmission and distribution system to improve system performance and reliability for its members.[162]

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[159] *See* Trans. at page 70, line 24 through page 71, line 16; page 90, line 7 through page 108, line 22; Exhibit A-4.

[160] The Commission does not have jurisdiction over the siting of this line. *See* A.R.S. §40-360, *et seq.*

[161] *See* Trans. at page 301 page 3 through page 309, line 17; *see* also late filed Exhibit A-26.

[162] Exhibit S-5 at page 7, lines 11-13, page 19, lines 18-20, and page 20, lines 7-8.

VI. CONCLUSION

Based upon the evidence presented at the hearing, SSVEC respectfully requests that the ALJ issue a ROO recommending that:

- SSVEC's Application be approved as modified herein.
- SSVEC has a Test Year original cost rate base of $132,886,202 and is entitled to an opportunity to earn a return on fair value rate base (margin) of 12.57.
- In order for SSVEC to achieve its financial and operational objectives, including the achievement of a 30 percent equity-to-long-term debt capitalization ratio by 2016, the Commission adopt SSVEC's proposed revenue requirement of $102,688,240 set forth in Section IV.A herein.
- SSVEC's proposed revenue requirement produces a net 2.46 operating TIER and a 2.25 DSC.
- The Commission finds that all of the issues set forth in Section III herein where the Cooperative and Staff are in agreement be adopted.
- Staff's revenue requirement adjustments set forth in Section IV.A.1-5 herein be denied. To the extent, however, that any of Staff's proposed adjustments are adopted for ratemaking purposes, the Commission should increase SSVEC's operating margin by a like amount to ensure that SSVEC's proposed revenue requirement is realized so the Cooperative will have sufficient revenue to achieve its financial and operational objectives.
- SSVEC should not be required to file for Commission approval of WPFCA increases. If, however, approval of WFPCA increases are required, that (i) such filings be limited to increases that will result in a cumulative annual increase in the total average rate collected from customers per kWh greater than 10 percent; (ii) increases should be limited to those increases that increase the WFPCA rate above the WPFCA factor in effect at the time SSVEC implements the new rates and charges pursuant to the Decision; (iii) power purchased from AEPCO that is passed through the Commission-approved AEPCO adjustor should not be considered for purposes of an increase to the WPFCA; (iv) once the Commission increases the adjustor per a filing by SSVEC, such new rate should be considered the ceiling for future filings; (v) the increase should automatically go into effect 60 days after the filing unless suspended by the Commission; and (vi) the $453,347 of DSM Program expenses for 2007 and 2008 to be included in the WPFCA not be considered for purposes of the $2 million under-collection threshold or for WPFCA adjustor increase calculations.
- The Cooperative not be required to file for a prudency review of its power procurement activities at the next rate case or within three years, whichever comes first.

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- The annual reset of the Cooperative's DSM adjustor should be deemed approved if the Commission does not act to suspend the Cooperative's filing by June 1.

- SSVEC be permitted to file for a DSM reset more than once a year if the Cooperative deems it to be necessary for the timely recovery of DSM Program expenses.

- The Commission adopt SSVEC's proposed Customer Charges.

- The Commission adopt SSVEC's proposed $50 charge for Regular Hour Connections and Regular Hour Non-Pay Trips.

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ATTACHMENT A

Commission Approved Rate Case Expenses

Utility	Docket No.	Decision No.	Date of Decision	Requested Rev. Requirement	Approx No. of Customers	Approved Rate Case Expenses	Amortization Period
UNS Electric	E-04204A-06-0783	70360	May 27, 2008	$171,631,367	93,000	$300,000	3
Arizona-American Water	W-01303A-07-0209	70351	May 16, 2008	$9,711,596	23,000	$94,264	4
UNS Gas	G-04204A-06-0463	70011	November 27, 2007	$178,393,000	140,000	$300,000	3
Far West Water and Sewer	WS-03478A-05-0801	69335	February 20, 2007	$1,900,786	5,500	$160,000	3
Black Mountain Sewer	SW-02361A-05-0657	69164	December 5, 2006	$1,375,037	1,957	$150,000	4
Arizona Water Company	W-01445A-04-0650	68302	November 14, 2005	$12,140,321	20,266	$250,000	3
Chaparral City Water	W-02113A-04-0616	68176	September 30, 2005	$7,795,935	12,000	$285,000	4
Pine Water Company	W-03512A-03-0279	67166	August 10, 2004	$922,984	2,000	$200,000	4
Arizona-American Water	WS-01303A-02-0867	67093	June 30, 2004	$10,331,873	15,000	$418,941	3
Arizona Water Company	W-01445A-02-0619	66849	March 19, 2004	$18,909,627	29,000	$250,000	3

SSVEC Rate Case

Requested Revenue Requirement	$103,495,149
Number of Customers	50,000
Requested Rate Case Expenses	$397,606
Amortization Period	5 Years
Staff Recommended Rate Case Expenses	$100,000

ATTACHMENT B

Sulphur Springs Valley Electric Cooperative, Inc.

A Touchstone Energy® Cooperative

Sonoita Reliability Project
SSVEC Rate Case E-01575A-08-0328

OPTIONS CONSIDERED AND COST ESTIMATES

SSVEC considered many options before making the final decision on where to build and what kind of system to build to ensure quality and reliable service to all of our members in the Sonoita/Elgin/Patagonia area.

- **Option 1: As Currently Planned**

  The route that SSVEC has chosen is the most cost-efficient route, affects the fewest members, and uses existing easements. The cost to build this route and substation is approximately $13.5 million. This route has been on record for more than a quarter of a century and is an established utility corridor. Other alternatives would cost approximately 1.8 to 4.1 times more than the $13.5 projected cost of this option.

- **Option 2: Following V7 Feeder – Energized (Hot)**

  This option upgrades the existing feeder line along Highway 82 and Elgin Road. Rebuilding the line energized would be slow, expensive, and dangerous to our linemen. In addition, it would require the acquisition of rights-of-way from more than 80 landowners, as the existing right-of-way does not include sub-transmission land rights. Furthermore, the majority of this route has been designated a part of the 2000 Las Cienegas Conversation Area and would require special permitting from the Bureau of Land Management. The cost of this option would be approximately $24.6 million.

- **Option 2A: Following V7 Feeder – De-Energized (Cold)**

  This option upgrades the existing feeder line along Highway 82 and Elgin Road. This option reflects the de-energized cost by building an adjacent line. Rebuilding this line by building an adjacent line to the current line, while safer for our linemen, will still require the rights-of-way mentioned in Option 2 above. The cost of this option is approximately $19.6 million.

- **Option 3: 69kV URD (Buried)**

  This option would follow the Option 1 "As Currently Planned" route - but with an underground (URD) 69 kV sub-transmission line. Although this option seems to be a simple solution (especially since many residential members have opted to install underground distribution lines), installing an underground sub-transmission line is a very complex task and significant issues are involved and is quite expensive. Those issues are:

  1. The insulated cables used in underground sub-transmission lines require one or two large trenches which lead to greater environmental disturbances. Also, concrete vaults or large manhole covers are required every 900 to 2,000 feet depending on terrain.
  2. Underground electric conductors produce heat, and, for efficient operation, this heat must me carried away from the conductors (air performs this function for overhead

lines). This requires special concrete caps around the soils and special thermal backfill material to move the heat away from the line.

3. The right-of-way must be kept clear of any vegetation due to the possible interference by root systems.
4. Studies have indicated the lifespan of underground conductors is half that of overhead, thus increasing costs over time.
5. Any failures in underground transmission lines are extremely costly, disruptive, and time expensive to repair. Underground outages can last for weeks and even months.

The estimated cost of underground 69kV sub-transmission line is estimated to cost approximately $55 million, plus the shorter life span and increased cost over time to repair.

- **<u>Option 4: To Buchanan on Babocomari</u>**

  This option would follow the Option 1 "As Currently Planned" route but would end the sub-transmission line at the Buchanan Substation site and build a new substation in the Sonoita Hills Subdivision. After input from the community, it was determined that moving this substation to an industrial/business location would impact less people. If SSVEC were to build on this site, it would require building not only a substation, but also one triple-circuit and one single-circuit large conductor feeder through the Sonoita Hills Subdivision. This option would cost approximately $13.3 million but was not chosen because for $200,000 more, we decided to move the substation and the lines to an industrial/business location.

- **<u>Option 5: TEP Interconnect - Interconnect to the TEP 46kV Sub-Transmission Line.*</u>**

  This TEP line was built in the 1940's. Several significant issues were identified with this alternative:

  1. This power line serves Fort Huachuca and does not have enough capacity available for a substation to carry the additional load of the Sonoita/Elgin/Patagonia area.
  2. TEP is bound through their Certificate of Convenience and Necessity by a special bonding arrangement which strictly limits their ability to serve outside two counties. TEP's management in 1993 and in 2007 indicated that a joint project may violate their bonding agreement.
  3. Additional rights-of-way adjacent to the TEP line would be required, which would be expensive.
  4. SSVEC's short-cost analysis also indicates that this option would be much more expensive than the chosen route .

** Option 5 is not a viable option, therefore, it was not fully estimated.*

Cost Summary for Sonoita Reliability Project Options					
Cost Category	**Option #1 As Currently Planned**	**Option #2 Following V7 Feeder (Hot)**	**Option #2A Following V7 Feeder (Cold)**	**Option #3 69kV URD**	**Option #4 To Buchanan on Babocomari**
Labor	$2,111,677	$4,678,210	$2,768,232	$14,651,321	$2,152,797
Materials	$4,315,260	$6,428,950	$6,123,620	$32,230,965	$5,048,297
Equipment & Rentals	$747,222	$1,951,193	$1,324,910	$1,852,193	$647,668
Transportation & Travel Costs	$504,914	$1,339,492	$937,946	$1,246,492	$467,038
Substation	$3,525,000	$3,875,000	$3,675,000	$3,875,000	$3,525,000
ROW & Fees	$686,435	$3,309,464	$3,138,653	$754,592	$86,539
Misc & Overhead	$1,622,657	$3,029,107	$1,709,135	$861,584	$1,389,225
Total	**$13,513,165**	**$24,611,416**	**$19,677,496**	**$55,472,147**	**$13,316,564**

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ATTACHMENT C

STAFF'S RESPONSES TO
SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE
FIRST SET OF DATA REQUESTS
DOCKET NO. E-01575A-08-0328
FEBRUARY 13, 2009

SSVEC 1.6 **Please provide a list of all utilities that are subject to an order from the Arizona Corporation Commission requiring that changes in the WPCA (or equivalent) rate be submitted to the Commission for approval. Please also provide the most recent decision number for each utility that sets forth the approval requirement.**

Response: For purposes of this response, Staff has assumed that the data request pertains only to electric utilities.

Ajo Improvement Company	Order Number not available in Commission database. Requirement instituted prior to 1977.
Morenci Water & Electric	Order No. 68438
Tucson Electric Power	Order No. 70628

In addition, three utilities submit adjustor changes to the Commission which go into effect unless suspended by the Commission. In two cases, annual caps are also imposed, as indicated below.

AEPCO	Order No. 68071
Arizona Public Service	Order No. 69663 (four mil annual cap). See also the Power Supply Adjustment Plan of Administration, filed 7/30/07.
UNS Electric	Order No. 70360 (1.73 cents per kWh annual cap)

Respondent: Julie McNeely-Kirwan